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Plain Meaning, the Tax Code, and Doctrinal Incoherence

by
MARY L. HEEN*

Introduction

The Supreme Court has turned increasingly to a “plain meaning” approach in statutory interpretation cases.¹ This approach poses special dangers for tax law because of the rich range of contextual and policy considerations that inform the Internal Revenue Code.² Under the plain meaning approach, the Court relies on the meaning of the

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1. See WILLIAM N. ESKRIDGE, JR., DYNAMIC STATUTORY INTERPRETATION 227 (1994) [hereinafter ESKRIDGE, DYNAMIC STATUTORY INTERPRETATION]; William N. Eskridge, Jr. & Philip P. Frickey, *The Supreme Court 1993 Term: Foreword: Law as Equilibrium*, 108 HARV. L. REV. 26, 58 nn.133-34 (1994) (noting that of the 56 decisions involving statutory interpretation in the 1993 term, the Court applied plain meaning as its primary source of interpretation in 24 cases; of the 36 cases involving statutes enacted in the last thirty years, the Court applied plain meaning in 20 cases).

2. Internal Revenue Code of 1986, as amended, 26 U.S.C. §§ 1-9806 [hereinafter Code]. See Deborah A. Geier, *Commentary, Textualism and Tax Cases*, 66 TEMP. L. REV. 445, 459-60 (1993) [hereinafter Geier, *Textualism*] (asserting that textualism may produce wrong results in cases implicating the structural framework and integrity of the income tax). See also Deborah A. Geier, *Interpreting Tax Legislation: The Role of Purpose*, 2 FLA. TAX REV. 492, 497-502 (1995) [hereinafter Geier, *Purpose*] (arguing that the overall structure of the Code must inform statutory interpretation, and, consequently, Code provisions should not be construed to damage the Code structure even if the interpretation is nonliteral); Michael Livingston, *Congress, the Courts, and the Code: Legislative History and the Interpretation of Tax Statutes*, 69 TEX. L. REV. 819, 822-23 (1991) (arguing that the plain meaning rule and legislative intent must be considered in light of the tax legislative process); Lawrence Zelenak, *Thinking About Nonliteral Interpretations of the Internal Revenue Code*, 64 N.C. L. REV. 623, 630 (1986) (arguing that nonliteral interpretations of the Code are appropriate when literal interpretation conflicts with Code policy or structure). *But see* Edward A. Zelinsky, *Text, Purpose, Capacity, and Albertson's: A Response to Professor Geier*, 2 FLA. TAX REV. 717 (1996) (critiquing the structural/social policy dichotomy suggested by Professor Geier). See generally Edward J. McCaffery, *Tax's Empire*, 85 GEO. L.

statutory words themselves rather than on legislative history, intent or purpose.³ This method of interpretation, closely associated with textualists such as Justice Antonin Scalia,⁴ is consistent with the view that the role of the judiciary is to interpret the text of the statute, enacted by Congress and signed into law by the President,⁵ and not to interpret the statute more generally in light of its legal or social context.⁶

J. 71, 137-40 (1996) (discussing a political-interpretive approach to tax policy analysis and comparing three modes of interpretation as illustrations of such an approach).

3. The Court sometimes consults legislative history to "confirm or rebut" the "plain meaning" of the statute. ESKRIDGE, *DYNAMIC STATUTORY INTERPRETATION*, *supra* note 1, at 227. At least in some cases, court holdings that have been labeled plain meaning decisions by some commentators may represent instances in which the language of the statute and the statutory purpose coincide. See T. Alexander Aleinikoff & Theodore M. Shaw, *The Costs of Incoherence: A Comment on Plain Meaning*, West Virginia Hosps., Inc. v. Casey, and *Due Process of Statutory Interpretation*, 45 VAND. L. REV. 687, 700-01 (1992). But see Frederick Schauer, *The Practice and Problems of Plain Meaning: A Response to Aleinikoff and Shaw*, 45 VAND. L. REV. 715, 717-22 (1992) [hereinafter Schauer, *Practice and Problems*] (discussing the impact of cases where plain meaning and statutory purpose diverge).

4. Under the textualist approach, the interpreter generally considers the statutory text, the structure of the statute and related statutory provisions, dictionary meanings, and certain linguistic canons of construction. For discussion and criticism of the textualist approach to statutory interpretation, see William N. Eskridge, Jr., *The New Textualism*, 37 UCLA L. REV. 621 (1990) (examining the new textualism of the 1980s); William D. Popkin, *An "Internal" Critique of Justice Scalia's Theory of Statutory Interpretation*, 76 MINN. L. REV. 1133 (1992) (criticizing Justice Scalia's text- and rule-based approach to decision making). See also, e.g., Stephen Breyer, *On the Uses of Legislative History in Interpreting Statutes*, 65 S. CAL. L. REV. 845 (1992) (defending the use of legislative history in statutory interpretation); Patricia M. Wald, *The Sizzling Sleeper: The Use of Legislative History in Construing Statutes in the 1988-89 Term of the United States Supreme Court*, 39 AM. U. L. REV. 277 (1990) (discussing how the use of legislative history implicates the roles of legislators and judges).

5. See U.S. CONST. art. I, § 7, cl. 2-3 (requiring bicameralism and presentment). See generally U.S. CONST. art. I-III (implying separation of powers). E.g., *Chisom v. Roemer*, 501 U.S. 380, 405 (1991) (Scalia, J., dissenting) ("We are to read the words of [the] text as any ordinary member of Congress would have read them . . . and apply the meaning so determined."); *Green v. Bock Laundry Mach. Co.*, 490 U.S. 504, 527-30 (1989) (Scalia, J., concurring) (articulating a plain meaning approach to statutory interpretation). See generally, ESKRIDGE, *DYNAMIC STATUTORY INTERPRETATION*, *supra* note 1, at 230-38 (critiquing the main constitutional justifications for the "new textualism," including the bicameralism and presentment and separation of powers arguments, and arguing that the textualist methodology "is no more objective or constraining than other methodologies").

6. Cf., e.g., T. Alexander Aleinikoff, *Updating Statutory Interpretation*, 87 MICH. L. REV. 20, 21-22 (1988) (arguing for a "nautical" approach to statutory interpretation, in which statutes are interpreted in light of current conditions, and distinguishing such a dynamic approach to interpretation from an "archaeological" approach, where a statute's meaning is fixed at the time of enactment); William N. Eskridge, Jr., *Dynamic Statutory Interpretation*, 135 U. PA. L. REV. 1479, 1479 (1987) (arguing for a dynamic approach in which statutes are interpreted in light of their current social, political and legal context); GUIDO CALABRESI, *A COMMON LAW FOR THE AGE OF STATUTES* 82, 163-66 (1982) (arguing for judicial power to nullify or modify obsolete statutes).

Although the textualists do not command a majority on the Court, the Court as a whole utilizes a plain meaning approach when the language of the statute is "unambiguous."⁷ In identifying such unambiguous or determinate language, the Court often refers to dictionary meanings of words,⁸ linguistic canons of construction,⁹ the way the specific provision being construed relates to the statute as a whole,¹⁰ or to other legislative enactments.¹¹

Commentators have speculated about the reasons for the trend toward increased use of the relatively acontextual plain meaning analysis. Professor Frederick Schauer suggests that the Court may use plain meaning as a "second best coordinating device," given a "lack of individual engagement in the outcome or nuances" of certain rela-

7. See *infra* notes 37-42 and accompanying text.

8. See, e.g., *Chapman v. United States*, 500 U.S. 453, 462 (1991) (relying on the dictionary definition of "mixture" in interpreting a federal criminal statute); Note, *Looking It Up: Dictionaries and Statutory Interpretation*, 107 HARV. L. REV. 1437, 1438 (1994) (finding that dictionary definitions were used in 28% of the published opinions during the Supreme Court's 1992 Term, a fourteen-fold increase over the 1981 Term).

9. See, e.g., *Leatherman v. Tarrant County Narcotics Intelligence and Coordination Unit*, 507 U.S. 163, 168 (1993) (applying the *expressio unius est exclusio alterius* canon, which can be translated as the expression of one thing implies the exclusion of the other); *Lukhard v. Reed*, 481 U.S. 368, 376 (1987) (plurality opinion) (observing that unlike the Internal Revenue Code and the food stamp statute, the AFDC statute contained no exclusion from income for personal injury awards, and thus welfare benefits were properly reduced to reflect the amount of a personal injury recovery). For a catalog of the Rehnquist Court's canons of statutory construction, see ESKRIDGE, *DYNAMIC STATUTORY INTERPRETATION*, *supra* note 1, at 323-28. See also Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to be Construed*, 3 VAND. L. REV. 395, 396 (1950) (listing mutually conflicting canons of statutory interpretation); Geoffrey P. Miller, *Pragmatics and the Maxims of Interpretation*, 1990 WIS. L. REV. 1179, 1190-91 (suggesting that maxims of interpretation possess features of considerable generality and are useful); David L. Shapiro, *Continuity and Change in Statutory Interpretation*, 67 N.Y.U. L. REV. 921, 925-26 (1992) (arguing that the use of canons fosters social stability); Cass R. Sunstein, *Interpreting Statutes in the Regulatory State*, 103 HARV. L. REV. 405, 413 (1989) (arguing that some disputes over meaning are in fact disputes over background norms such as constitutional principles and contemporary institutional arrangements); See generally Symposium, *A Reevaluation of the Canons of Statutory Interpretation*, 45 VAND. L. REV. 529-795 (1992).

10. See, e.g., *Conroy v. Aniskoff*, 507 U.S. 511, 515 (1993) (observing the "cardinal rule" that statutes are to be read as a whole); *Mass. v. Morash*, 490 U.S. 107, 115 (1989) (noting that the Court is guided by looking at provisions of the statute as a whole); *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs.*, 484 U.S. 365, 371 (1988) ("[a] provision that may seem ambiguous in isolation is often clarified by the remainder of the statutory scheme").

11. See, e.g., *West Virginia Univ. Hosps., Inc. v. Casey*, 499 U.S. 83, 88-92 (1991) (construing a statute providing for attorney's fees in civil rights cases by referring to other statutes); *Pierce v. Underwood*, 487 U.S. 552, 564-65 (1988) (interpreting a statute by referring to two other legislative enactments).

tively uninteresting cases and the "desire to reach some agreement for the sake of agreement."¹² Others point to the influence of Justice Scalia's textualist views on other members of the Court¹³ or, alternatively, to a pragmatic effort by opinion writers for Justice Scalia's vote.¹⁴ Many others believe that the Court frequently exaggerates the clarity of a statute,¹⁵ in order to use the plain meaning doctrine to impose its own views, all the while paying lip service to separation of powers.¹⁶

Whatever the reasons for the Court's increased reliance on the plain meaning approach, its use depends upon a judicial determination that the statutory provision being interpreted is not ambiguous. Whether the language of a statute is ambiguous or not may depend upon the background and knowledge of the interpreter¹⁷ as well as the

12. See Schauer, *Practice and Problems*, *supra* note 3, at 722-23. See also Frederick Schauer, *Statutory Construction and the Coordinating Function of Plain Meaning*, in 1990 THE SUPREME COURT REVIEW 231, 250-56 (Gerhard Casper et al., eds., 1991) [hereinafter Schauer, *Coordinating Function*] (arguing that the Court uses the plain meaning in statutory interpretation cases as a second-best solution, to "agree about what the language they all share requires").

13. See ESKRIDGE, *DYNAMIC STATUTORY INTERPRETATION*, *supra* note 1, at 226-29.

14. See JERRY L. MASHAW, *Textualism, Constitutionalism, and the Interpretation of Federal Statutes*, 32 WM. & MARY L. REV. 827, 833 (1991) ("One should not discount, however, the way in which the dynamics of majority-making may push litigants, lower courts, and other Justices in the direction staked out by Justices Scalia and Kennedy.").

15. E.g., NICHOLAS S. ZEPPOS, *Justice Scalia's Textualism: The "New" New Legal Process*, 12 CARDOZO L. REV. 1597, 1623-27 (1991) (showing specific instances where Justice Scalia's textualism masked the policy choices which are "inevitable in difficult statutory interpretation cases").

16. See, e.g., RICHARD J. PIERCE, JR., *The Supreme Court's New Hypertextualism: An Invitation to Cacophony and Incoherence in the Administrative State*, 95 COLUM. L. REV. 749, 779-81 (1995) (hypothesizing that post-*Chevron* textualism masks political conservatism and ideology); MURIEL MORISEY SPENCE, *The Sleeping Giant: Textualism As Power Struggle*, 67 S. CAL. L. REV. 585, 593-97 (1994) (arguing that textualism creates interbranch conflict); NICHOLAS S. ZEPPOS, *Legislative History and the Interpretation of Statutes: Toward a Fact-Finding Model of Statutory Interpretation*, 76 VA. L. REV. 1295, 1323-35 (1990) (suggesting that the textualist is attempting to correct shortcomings in the legislative process through judicial activism). See also NICHOLAS S. ZEPPOS, *Judicial Candor and Statutory Interpretation*, 78 GEO. L.J. 353, 411 (1989) (observing that the problem is not so much a "lack of candor in statutory interpretation, but a lack of self-awareness in judging" and questioning the desirability of increased judicial candor).

17. See ESKRIDGE, *DYNAMIC STATUTORY INTERPRETATION*, *supra* note 1, at 58-68 (discussing Gadamer's *Truth and Method*); WILLIAM N. ESKRIDGE, JR., *Gadamer/Statutory Interpretation*, 90 COLUM. L. REV. 609, 617 (1990) ("Interpretation is the common ground of interaction between text and interpreter. . ."). For some of the substantial literature on legal hermeneutics, see *A Symposium on Legal and Political Hermeneutics*, 16 CARDOZO L. REV. 1879 (1995); *Interpretation Symposium: Hermeneutics and Legal Interpretation*, 58 S. CAL. L. REV. 199 (1985); FRANCIS J. MOOTZ, III, *The Ontological Basis of Legal Hermeneutics: A Proposed Model of Inquiry Based on the Work of Gadamer, Habermas, and*

skill of the drafter.¹⁸ It may also depend upon the sources consulted to aid in interpretation.

Statutes develop over a period of time and in response to the active interrelationship among decisions of the administrative agencies, the courts, and Congress.¹⁹ As Professor Edward Rubin and others point out, some statutes are directed to bureaucracies or agencies charged with enforcing complex regulatory provisions.²⁰ Some are enacted in response to court decisions or with the legislative expectation that courts will fill in statutory gaps when unanticipated questions arise.²¹ A specialized interpretive community may rely on meanings for words or phrases that develop over time in a particular regulatory context.²²

Ricoeur, 68 B.U. L. REV. 523 (1988); Gary C. Leedes, *The Latest and Best Word on Legal Hermeneutics: A Review Essay of Interpreting Law and Literature: A Hermeneutic Reader*, 65 NOTRE DAME L. REV. 375 (1990) (book review). See also Peter C. Schanck, *Understanding Postmodern Thought and its Implications for Statutory Interpretation*, 65 S. CAL. L. REV. 2505 (1992) (detailing the philosophical premises of postmodernism and arguing that these ideas have a profound influence on statutory interpretation).

18. See Zelinsky, *supra* note 2, at 730-33 (acknowledging that "there is plenty of ambiguity in the Code, stemming . . . from political compromise, poor draftsmanship, deliberate and implicit delegation to the courts and tax administrators, and the inherent limitations of language").

19. See Eskridge & Frickey, *supra* note 1, at 56-76; William N. Eskridge, Jr. & John Ferejohn, *The Article I, Section 7 Game*, 80 GEO. L.J. 523, 559-64 (1992).

20. See Edward L. Rubin, *Law and Legislation in the Administrative State*, 89 COLUM. L. REV. 369, 380 (1989) (explaining that modern legislation "consists of directives to implementation mechanisms"); Colin S. Diver, *Statutory Interpretation in the Administrative State*, 133 U. PA. L. REV. 549, 551-52 (1985) (distinguishing statutes addressed to government agencies from those addressed to private persons and arguing that courts should defer to agency interpretations when the agency has the authority to set policy). See also Michael Herz, *Textualism and Taboo: Interpretation and Deference for Justice Scalia*, 12 CARDOZO L. REV. 1663, 1673-76 (1991) (suggesting that Justice Scalia's textualism and the *Chevron* doctrine reflect the divergent interpretive approaches applied by courts and policymaking agencies); Peter L. Strauss, *Legislative Theory and the Rule of Law: Some Comments on Rubin*, 89 COLUM. L. REV. 427, 442-44 (1989) (accepting Rubin's description of the problems posed by legislation and suggesting new systemic theories for solving separation of powers problems).

21. See William D. Popkin, *The Collaborative Model of Statutory Interpretation*, 61 S. CAL. L. REV. 541, 590-626 (1988). See also Myron C. Grauer, *A Case for Congressional Facilitation of a Collaborative Model of Statutory Interpretation in the Tax Area: Lessons to be Learned from the Corn Products and Arkansas Best Cases and the Historical Development of the Statutory Definition of "Capital Asset(s)"*, 84 KY. L.J. 1, 4-7 (1995-96) (suggesting methods of drafting that Congress could use in order to facilitate collaboration with the courts).

22. See Samuel B. Sterrett, *Use of Industry Definitions in Interpretation of the Internal Revenue Code: Towards a More Systematic Approach*, 16 VA. TAX REV. 1, 29-35 (1996) (arguing that the Court should use the readily known or "industry definition" of technical terms having a specific meaning outside of the context of the Code). For a discussion of

An acontextual determination by the Court of the threshold question of whether a statute is ambiguous presents the possibility that a complex statute may be misinterpreted by the Court.²³ Therein lies the inherent limitation of the plain meaning approach. That limitation has been acknowledged even by defenders of the plain meaning approach: "Plain meaning, quite simply, is a blunt, frequently crude, and certainly narrowing device, cutting off access to many features of some particular conversational or communicative or interpretive context that would otherwise be available to the interpreter or conversational participant."²⁴

The plain meaning approach also creates a heightened risk of error because of its relationship to agency deference under *Chevron, USA, Inc. v. Natural Resources Defense Council, Inc.*²⁵ Under the *Chevron* doctrine, reviewing courts must defer to an agency's reasonable interpretation of an ambiguous statute. However, under the Court's expanding use of plain meaning analysis, the Court less frequently finds statutory language to be ambiguous. In the tax context, the plain meaning approach not only cuts the Court off from the Code's interpretive context and policy background but also makes deference to Treasury's expertise less likely.²⁶

This Article examines the Supreme Court's interpretive approach in recent tax cases. Part I of the Article sets the stage by describing the Court's interpretive approach, its focus on the relative determinacy of statutory language, and the backdrop of *Chevron*. Part II examines the effect of these issues on tax law, focusing on three cases that construe the same Code provision, section 104(a)(2),²⁷ but apply

the nature of technical language, see Mary Jane Morrison, *Excursions into the Nature of Legal Language*, 37 CLEV. ST. L. REV. 271 (1989).

23. See Gwen T. Handelman, *Zen and the Art of Statutory Construction: A Tax Lawyer's Account of Enlightenment*, 40 DEPAUL L. REV. 611, 622-32 (1991).

24. Schauer, *Coordinating Function*, *supra* note 12, at 252.

25. 467 U.S. 837 (1984).

26. See Geier, *Textualism*, *supra* note 2, at 460 (suggesting that textualism takes away the authority of the courts and the Treasury Department to interpret the Code in ways that protect its structural integrity). See *infra* discussion at Part I.B.

27. In all three cases, see *infra* Part II, the Supreme Court interpreted the scope of § 104(a)(2) of the Internal Revenue Code. During the period relevant to the three cases, that section provided in pertinent part as follows:

Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, gross income does not include—

...

quite different interpretive approaches. In *United States v. Burke*,²⁸ the Court appeared to find the provision ambiguous and relied in part upon an interpretation of the statute contained in a Treasury regulation.²⁹ Subsequently, in *Commissioner v. Schleier*,³⁰ the Court applied a plain meaning analysis to find an additional "independent" statutory requirement.³¹ Most recently, in *O'Gilvie v. United States*,³² the Court acknowledged the existence of a linguistic ambiguity in the same language interpreted by the Court in *Schleier* and construed it by reference to a contextual examination of the history and tax-related purpose of the provision.³³ The inconsistency of the analysis in these cases is evidence that the Court's evolving approach to statutory interpretation is doctrinally unstable. Moreover, a close reading of the cases reveals unresolved doctrinal conflicts regarding the scope and meaning of the Code provision. Although those conflicts have now been largely resolved by Congress in legislation enacted last summer,³⁴ the cases illustrate the doctrinal incoherence that can result from or be intensified by the Court's inconsistent approaches to its interpretive task.

Part III outlines some of the normative questions that must be addressed if the Court continues on its present course, including an evaluation of the costs of relying on legislative "correction." When the Court discerns plain meaning, it analyzes the statute without consideration of extrinsic contextual sources of interpretation and without deference to the administrative agency charged with its enforcement. Professor Schauer argues that this approach is a norma-

(2) the amount of any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injuries or sickness;

Internal Revenue Code of 1986 § 104(a), as amended, 26 U.S.C. § 104(a) (West Supp. 1989). In two of the cases, the Court decided whether the exclusion from gross income for amounts received on account of personal injuries encompasses certain employment discrimination recoveries. Each time, the Court acknowledged that employment discrimination could constitute a "personal injury" within the meaning of the statute but held that the particular sex- and age-based discrimination recoveries received by the taxpayers were not excludable from gross income. In the third case, the Court held that the exclusion "on account of" personal injuries did not encompass punitive damage awards for physical injuries. For a complete discussion of the cases, see *infra* Part II.

28. 504 U.S. 229 (1992).

29. *See id.* at 234.

30. 115 S. Ct. 2159 (1995).

31. *See id.* at 2164-67.

32. 117 S. Ct. 452 (1996).

33. *See id.* at 457-58.

34. *See* Small Business Job Protection Act of 1996, Pub. L. No. 104-188, § 1605, 110 Stat. 1755 (1996). For further discussion, see *infra*, Part III.

tively beneficial and efficient decision-making model for a Court with such diverse political and jurisprudential outlooks³⁵ and that it also protects the public from captured administrative agencies.³⁶ The question remains whether the costs of incoherence in a complex statutory scheme outweigh these supposed benefits.

Although it may be too early to tell what the costs will be for the development of tax law, the preliminary evidence suggests that the "benefit" of less engagement by the Court in the substantive issues may not be worth the risk of increased doctrinal incoherence. The Court may reach sounder decisions more often with a deeper engagement in the details of the statute and through a wider ranging consideration of its historical, structural, and policy context. Alternatively, consideration by the Court of these contextual sources of interpretation may more frequently result in a finding of statutory ambiguity or indeterminacy, leading to deference to the expertise of Treasury.

I. The Court's Interpretive Approach: Plain Meaning and the Backdrop of *Chevron*

The Supreme Court claims that it applies the plain meaning approach when it finds the language of the statute to be unambiguous.³⁷ Determining whether language is ambiguous or not itself involves interpretation. Justice Scalia often emphasizes that "plain meaning" involves finding the "ordinary" meaning of words in their textual context.³⁸ Determinacy is a matter of degree, and because even "ordi-

35. Schauer, *Coordinating Function*, *supra* note 12, at 253-56.

36. Professor Schauer explains the concern about regulatory capture as follows: Surely we can understand the plausibility of Rubin's worry about outsider courts using techniques such as reading the statutes as outsiders to interfere excessively with the ongoing and arguably family-like relationship between agency and legislature. But so too might we understand the plausibility of courts worrying that sometimes-captured agencies with a practical last word on many issues might overassess or overclaim their own place in the governmental family. If and when this concern is plausible, courts viewing themselves as delegated agents of the legislature might see their role as one of enforcing the language of a statute against the efforts of an agency to bend that language to its own will.

Schauer, *Practice and Problems*, *supra* note 3, at 736 (footnotes omitted).

37. See, e.g., *Estate of Cowart v. Nicklos Drilling Co.*, 505 U.S. 469, 475 (1992) ("In a statutory construction case, the beginning point must be the language of the statute, and when a statute speaks with clarity to an issue judicial inquiry into the statute's meaning, in all but the most extraordinary circumstance, is finished."); *Demarest v. Manspeaker*, 498 U.S. 184, 190 (1991) (unanimous decision) ("When we find the terms of a statute unambiguous, judicial inquiry is complete except in rare and exceptional circumstances.")

38. I thought we had adopted a regular method for interpreting the meaning of language in a statute: first, find the ordinary meaning of the language in its textual context; and second, using established canons of construction, ask whether

nary” usage may result in two or more plausible linguistic interpretations of a text, members of the Court sometimes disagree on whether or not the language is plain.³⁹

Plainness may be influenced by the sources consulted and the identity of the presumed interpretive community.⁴⁰ The presumed interpretive community may be ordinary citizens, bureaucrats, non-specialist lawyers or judges, or specialists. It is not unusual in tax law, for example, for words to develop specialized meanings that differ from their ordinary usage.⁴¹ In addition, the reason or reasons for applying the plain meaning approach may affect an individual Justice’s relative willingness to find determinacy in the face of conflicting evidence of a contrary purpose or unintended results.⁴² The Court’s

there is any clear indication that some permissible meaning other than the ordinary one applies. If not—and especially if a good reason for the ordinary meaning appears plain—we apply that ordinary meaning.

Chisom v. Roemer, 501 U.S. 380, 404 (1991) (Scalia, J., dissenting).

For a discussion of the distinction between “unambiguous meaning” and “ordinary meaning” understandings of “plain meaning,” see Clark D. Cunningham et al., *Plain Meaning and Hard Cases*, 103 YALE L.J. 1561, 1563-66 (1994) (reviewing LAWRENCE M. SOLAN, *THE LANGUAGE OF JUDGES* (1993)). See also George H. Taylor, *Structural Textualism*, 75 B.U. L. REV. 321, 325-27 (1995) (distinguishing the “best case” for textualism from standard notions of “plain meaning”).

39. For a discussion of cases in which the Court has split over the “plain meaning” of statutory language, see LAWRENCE M. SOLAN, *THE LANGUAGE OF JUDGES* 101-04 (1993) (applying a linguistic analysis and arguing that the Court has become increasingly and mistakenly dogmatic about the lack of ambiguity in statutes). Solan identifies several sources of potential ambiguity in statutes, including (i) structural ambiguity caused by the relationship of words in a sentence structure, (ii) multiple interpretations of particular words, *id.* at 64, and (iii) problems of categorization, *id.* at 94-99, which “result from the imperfect match between concepts conveyed by the words in a statute and the virtually infinite variety of events that can occur in the world.” *Id.* at 105-06.

40. See STANLEY FISH, *IS THERE A TEXT IN THIS CLASS? THE AUTHORITY OF INTERPRETIVE COMMUNITIES* 305-21 (1980) (suggesting that meaning is the current determination of the relevant interpretive community based on each individual’s life experience).

41. For example, in tax law, ordinary words such as “realization” and “basis” have specialized meanings used in determining the tax consequences of dealings in property. See Code §§ 1012 (defining basis by reference to “cost” of the property), 1016 (providing for adjustments to basis), 1001(b) (defining amount realized from sale or disposition of property). See also Code §§ 1221 (defining capital assets), 1231 (defining § 1231 gains and losses for property used in a trade or business and for certain involuntary conversions).

For a discussion of tax rule indeterminacy and the use of highly specific language, see John A. Miller, *Indeterminacy, Complexity, and Fairness: Justifying Rule Simplification in the Law of Taxation*, 68 WASH. L. REV. 1, 40-43 (1993).

42. For example, if Justice Scalia, a textualist, applies plain meaning due to the constitutional requirements of bicameralism and presentment, he would be inclined not to depart from the plain meaning of the text to take into account contrary evidence of meaning in legislative history. See *supra* notes 3-6. By contrast, although Justice Stevens has relied on plain meaning in interpreting statutes, he is willing to consider contrary evidence of meaning in the legislative history because he finds helpful the traditional tools of statutory

struggle with its interpretive task thus has often focused on what sources of meaning will be consulted by the Court.

In the background of any discussion of plain meaning in statutory interpretation cases involving administrative agencies lurks the *Chevron* doctrine and more than a decade of controversy⁴³ and inconsistent applications.⁴⁴ The following section briefly describes the *Chevron* doctrine and then discusses its application by the Court in tax cases.

A. The *Chevron* Doctrine

In *Chevron*, the Court adopted a two-step approach for judicial review of administrative agency interpretation of statutes.⁴⁵ In the first step, the reviewing court determines whether Congress has expressed a clear intention regarding the "precise question at issue."⁴⁶ If so, the "court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."⁴⁷ If the statute is silent or ambiguous, the court proceeds to the next step. Under the second step, the court defers to the agency's interpretation of the statute unless it finds the agency's interpretation to be unreasonable.⁴⁸

construction as a means of ascertaining legislative intent. See *infra* notes 54-60 and accompanying text. See generally, e.g., Cass R. Sunstein, *Problems with Rules*, 83 CAL. L. REV. 953, 985 (1995) [hereinafter Sunstein, *Problems with Rules*] (discussing the moral and political dimension of views about what the law means and observing that "when prevailing views change, judgments of meaning, even of relatively plain meaning, may shift as well").

43. E.g., Cynthia R. Farina, *Statutory Interpretation and the Balance of Power in the Administrative State*, 89 COLUM. L. REV. 452, 456 (1989) (arguing that the *Chevron* doctrine requires a recasting of separation of powers and legitimacy principles); Cass R. Sunstein, *Law and Administration After Chevron*, 90 COLUM. L. REV. 2071, 2074-85 (1990) [hereinafter Sunstein, *Law and Administration*] (describing *Chevron* as "counter-Marbury" by requiring courts to play a more adaptive role in the administrative state, and observing that the principle of deference to agency interpretations of statutes has "produced considerable controversy"). But see Thomas W. Merrill, *Judicial Deference to Executive Precedent*, 101 YALE L.J. 969, 970 (1992) [hereinafter Merrill, *Judicial Deference*] (challenging the view that *Chevron* functions as a "counter-Marbury" because the Court has not strictly applied its all-or-nothing approach).

44. See Merrill, *Judicial Deference*, *supra* note 43, at 981-83 (finding in an empirical study that the Supreme Court applied *Chevron* in about one-third of the cases during the 1984-1990 terms, and one-half of the cases during the 1987-1990 terms, in which the Court reviewed agency interpretations of statutes); Pierce, *supra* note 16, at 750 (stating that "post-*Chevron* jurisprudence is so confused that it is difficult to determine what remains of the original, highly deferential test"). See also Peter H. Schuck & E. Donald Elliott, *To the Chevron Station: An Empirical Study of Federal Administrative Law*, 1990 DUKE L.J. 984, 1029-36 (reporting empirical data concerning the effect of *Chevron* on lower court review of agency decisions).

45. 467 U.S. 837, 842-44 (1984).

46. *Id.* at 842.

47. *Id.* at 842-43.

48. *Id.* at 843-44.

The *Chevron* doctrine can be viewed as a “new default presumption that Congress implicitly assigns agencies authority to resolve ambiguities in the statutes the agencies administer.”⁴⁹ The Court explained in *Chevron* that its deference to administrative agencies is consistent with our constitutional system, which vests policy-making discretion in more expert, representative, and politically accountable executive agencies.⁵⁰ The President and executive branch have power to resolve statutory ambiguities or gaps in accordance with the administration’s agenda.⁵¹

The Court has not reached a stable consensus concerning how reviewing courts determine whether a statute is silent or ambiguous. In tracing the evolution of the Supreme Court’s step one analysis, Professor Merrill has found that although the Court has been somewhat inconsistent, it has shifted from a focus on whether Congress expressed a “specific intention,” to whether the statute is “‘ambiguous’ or ‘unclear,’” and finally to whether the statute has a “plain meaning,” with no reference to “the precise question at issue.”⁵² Merrill argues that “there are signs that *Chevron* is being transformed by the Court into a new judicial mandate ‘to say what the law is.’”⁵³

Along with the shift in formulation, the Justices disagree about step one methodology. Justice Stevens, for example, usually relies upon “traditional tools of statutory construction,” including legislative

49. John F. Manning, *Constitutional Structure and Judicial Deference to Agency Interpretations of Agency Rules*, 96 COLUM. L. REV. 612, 625 (1996). See also Sunstein, *Law and Administration*, *supra* note 43, at 2119 (concluding that the “*Chevron* principle does not apply unless Congress has given law-interpreting power to the agency”). But see Dan M. Kahan, *Is Chevron Relevant to Federal Criminal Law?*, 110 HARV. L. REV. 469, 490-92 & n.125 (1996) (arguing for the *Chevronizing* of federal criminal law even though Congress hasn’t delegated to the Justice Department the authority to engage in interpretive lawmaking with respect to general criminal statutes).

50. *Chevron*, 467 U.S. at 865-66. For an extensive discussion of this rationale, see Jane S. Schacter, *Metademocracy: The Changing Structure of Legitimacy in Statutory Interpretation*, 108 HARV. L. REV. 593 (1995).

51. See, e.g., *Rust v. Sullivan*, 500 U.S. 173, 183-87 (1991) (noting that an agency’s construction of an ambiguous statute is not to be disturbed if it does not conflict with congressional intent, and that a prior agency interpretation may be reversed by the agency due to “changing circumstances”).

52. Merrill, *Judicial Deference*, *supra* note 43, at 990-91. For a recent example of the Court’s articulation of the “plain meaning” formulation, see *Holly Farms Corp. v. NLRB*, 116 S. Ct. 1396, 1401 (1996) (“If a statute’s meaning is plain, the Board and reviewing courts ‘must give effect to the unambiguously expressed intent of Congress.’”) (quoting *Chevron*, 467 U.S. at 843).

53. Merrill, *Judicial Deference*, *supra* note 43, at 970 (quoting *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803)).

history, to determine statutory meaning.⁵⁴ Justice Scalia, on the other hand,⁵⁵ argues that the use of traditional tools of statutory construction at step one would eviscerate *Chevron*, making deference “a doctrine of desperation, authorizing courts to defer only if they would otherwise be unable to construe the enactment at issue.”⁵⁶

As a textualist, Justice Scalia objects to the examination of legislative history to determine Congressional intent.⁵⁷ As a practical matter, however, Justice Scalia’s textualist approach may result in less frequent deference to agency interpretation of statutes.⁵⁸ Although

54. See, e.g., *INS v. Cardoza-Fonseca*, 480 U.S. 421, 443-46 (1987) (overturning the Attorney General’s interpretation of a provision of the Immigration and Naturalization Act). See also William D. Popkin, *A Common Law Lawyer on the Supreme Court: The Opinions of Justice Stevens*, 1989 DUKE L.J. 1087, 1136-60. Professor Popkin observes that, in tax cases, Justice Stevens has tended to adhere closely to statutory language because of the importance of consistent administration and “taxpayer reliance on fixed rules.” *Id.* at 1158. Where the language of the Code is not clear, however, Justice Stevens “appears ready to adopt an interpretation that prevents tax avoidance.” *Id.* at 1158 n.368. The opinion by Justice Stevens in *Commissioner v. Schleier*, 115 S. Ct. 2159 (1995), is generally consistent with those observations. See *infra* Part II.

55. See generally Popkin, *supra* note 4, at 1133-36 (comparing Justice Stevens’ intent-based case-by-case approach to statutory interpretation with Justice Scalia’s text and rule-based approach).

56. *Cardoza-Fonseca*, 480 U.S. at 454 (Scalia, J., concurring).

57. E.g., *United States v. Thompson/Center Arms Co.*, 504 U.S. 505, 521 (1992) (Scalia, J., concurring) (criticizing the plurality for “resort[ing] to that last hope of lost interpretive causes, that St. Jude of the hagiology of statutory construction, legislative history”); *Green v. Bock Laundry Mach. Co.*, 490 U.S. 504, 527 (1989) (Scalia, J., concurring) (criticizing the majority for devoting four-fifths of its substantive analysis to the evolution and legislative history of a Federal Rule of Evidence); *Blanchard v. Bergeron*, 489 U.S. 87, 97-100 (1989) (Scalia, J., concurring in part and in the judgment) (refusing to join that part of the majority opinion that analyzed lower court opinions referred to in the legislative history); *Hirschey v. Federal Emergency Reg. Comm’n*, 777 F.2d 1, 6-8 (D.C. Cir. 1985) (Scalia, J., concurring) (voicing concern that routine deference to the details of committee reports and the predictable expansion of such detail “are converting a system of judicial construction into a system of committee-staff prescription”); ANTONIN SCALIA, *A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW* 29-30 (1997) (stating that “legislative history should not be used as an authoritative indication of a statute’s meaning”).

58. Justice Scalia explains this result as follows:

One who finds *more* often (as I do) that the meaning of a statute is apparent from its text and from its relationship with other laws, thereby finds *less* often that the triggering requirement for *Chevron* deference exists. It is thus relatively rare that *Chevron* will require me to accept an interpretation which, though reasonable, I would not personally adopt. Contrariwise, one who abhors a “plain meaning” rule, and is willing to permit the apparent meaning of a statute to be impeached by legislative history, will more frequently find agency-liberating ambiguity . . .

Antonin Scalia, *Judicial Deference to Administrative Interpretations of Law*, 1989 DUKE L.J. 511, 521.

But see William N. Eskridge, Jr., *Reneging on History? Playing the Court/Congress/President Civil Rights Game*, 79 CAL. L. REV. 613, 679-80 & n.301 (1991) (citing Justice Scalia’s explanation and arguing that textualists have engaged in false modesty about the

Justice Scalia's views have gained some ground on the Court,⁵⁹ the role of legislative history and the use of other traditional tools of statutory construction in the *Chevron* framework remain unclear.⁶⁰

Other important issues concerning the application of *Chevron* include the type and format of administrative interpretations to which courts should apply *Chevron*,⁶¹ and the meaning and scope of the

subordinate role of the Court in statutory policy-making); Geier, *Textualism*, *supra* note 2, at 457 (questioning the "accepted wisdom" that Justice Scalia is a supporter of *Chevron* deference); Thomas W. Merrill, *Textualism and the Future of the Chevron Doctrine*, 72 WASH. U. L.Q. 351, 372 (1994) [hereinafter Merrill, *Textualism*] (arguing that the textualist approach is "incompatible with an attitude of deference toward other institutions—whether the other institution is Congress or an administrative agency"). *Contra* Gregory E. Maggs, *Reconciling Textualism and the Chevron Doctrine: In Defense of Justice Scalia*, 28 CONN. L. REV. 393 (1996) (arguing that textualism and the *Chevron* doctrine are not in conflict).

59. *E.g.*, *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281, 291 (1988) (in ascertaining plain meaning, "the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole") (citations omitted).

60. *See* *Dunn v. Commodity Futures Trading Commission*, 117 S. Ct. 913, 920 n.14 (1997) (Stevens, J.) (restating the principle stated by the Court in *Smiley v. Citibank*, 116 S.Ct. 1730, 1733 (1996), that "*Chevron* deference arises out of background presumptions of Congressional intent"). *Compare* *City of Chicago v. Environmental Def. Fund*, 114 S. Ct. 1588, 1594 (1994) (Scalia, J.) (concluding that the statute's text required rejection of the agency's interpretation, which went beyond the scope of whatever ambiguity the statute contained); *National R.R. Passenger Corp. v. Boston & Maine Corp.*, 503 U.S. 407 (1992) (Kennedy, J.) (using dictionary definitions to find ambiguity and deferring to the agency's interpretation); *Sullivan v. Everhart*, 494 U.S. 83, 89 (1990) (Scalia, J.) (applying the *Chevron* framework and deferring to an agency interpretation of the statute) *with* *Holly Farms v. NLRB*, 116 S. Ct. 1396, 1401 n.6 (1996) (Ginsburg, J.) (referring to the legislative history and purpose of the statute and concluding that the Board's interpretation of an ambiguous provision was "reasonable"); *Babbitt v. Sweet Home Chapter of Communities for a Great Or.*, 115 S. Ct. 2407 (1995) (Stevens, J.) (examining legislative history and statutory purpose to find Department of Interior regulation "reasonable"). *See* Merrill, *Textualism*, *supra* note 58, at 355-56 (noting the decrease, but not the elimination of, the use of legislative history). *See also* Merrill, *Judicial Deference*, *supra* note 43, at 984-85, 988-89 (documenting *Chevron*'s inconsistent application and suggesting that *Chevron* may be a mere canon of construction); Sunstein, *Law and Administration*, *supra* note 43, at 2105-19 (arguing that deference is one among many interpretive principles or norms used in statutory construction).

61. *E.g.*, Robert A. Anthony, *Interpretive Rules, Policy Statements, Guidances, Manuals, and the Like—Should Federal Agencies Use Them to Bind the Public?*, 41 DUKE L.J. 1311 (1992) (noting the different types of agency interpretive formats and their appropriate use); Robert A. Anthony, *Which Agency Interpretations Should Bind Citizens and the Courts?*, 7 YALE J. ON REG. 1, 4 (1990) (discussing "whether Congress intended to delegate to the agency the power to interpret with the force of law in the particular format that was used"); Sunstein, *Law and Administration*, *supra* note 43, at 2093-2104 (discussing deference to legislative rules, agency law-declaring as opposed to law-applying, issues of agency jurisdiction, agency bias, and departures from past practices). *See also* *Reno v. Koray*, 115 S. Ct. 2021, 2026-27 (1995) (citing *Chevron* and stating that an internal agency guideline of the Bureau of Prisons was entitled to "some deference" since it constituted a "permissible

“reasonableness” standard in step two of the *Chevron* framework.⁶² When the Supreme Court resolves statutory interpretation cases at step one, questions involving application of the “reasonableness” standard are frequently not addressed.⁶³ A plain meaning analysis at step one generally results in less acceptance by the Court of agency views than under the pre-*Chevron* approach.⁶⁴ However, when the Supreme Court does apply the two-step *Chevron* framework, it more often than not has deferred to the agency’s interpretation.⁶⁵

B. The Court’s Application of *Chevron* in Tax Cases

Although *Chevron* has been cited by the Supreme Court in a few tax cases,⁶⁶ *Chevron* has not had the same influence in the tax world

construction of the statute” (citations omitted)); *Shalala v. Guernsey Memorial Hosp.*, 115 S. Ct. 1232, 1240 (1995) (deferring to an agency interpretation of its own regulation).

62. E.g., Michael Herz, *Deference Running Riot: Separating Interpretation and Law-making Under Chevron*, 6 ADMIN. L. J. AM. U. 187, 210-12 (1992) (arguing that judicial review under step two should apply to agency interpretations made pursuant to an express delegation of interpretive authority); Mark Seidenfeld, *A Syncopated Chevron: Emphasizing Reasoned Decisionmaking in Reviewing Agency Interpretations of Statutes*, 73 TEX. L. REV. 83, 125-38 (1994) (arguing for increased emphasis on step two of *Chevron* and more scrutiny of the reasonableness of agency interpretation).

63. See Merrill, *Textualism*, *supra* note 58, at 362 (“The currently fashionable approach . . . is for the Court to . . . find that the statutory meaning is unambiguous, and then drop a footnote indicating that there is no need to consider deference to agency views.”); Pierce, *supra* note 16, at 750 (observing that the Court “gradually ceased to apply step two of the *Chevron* test . . . because it rarely acknowledges the existence of ambiguity”).

64. See Merrill, *Textualism*, *supra* note 58, at 362 (noting that *Chevron*’s potential deference effects are “largely an illusion” because of the increased use of step one resolutions); Merrill, *Judicial Deference*, *supra* note 43, at 984 (“Paradoxically, it appears that adoption of the *Chevron* framework has meant, if anything, a decline in deference to agency views.”).

65. Merrill, *Textualism*, *supra* note 58, at 359-60 (showing empirical data supporting agency deference in *Chevron* framework cases, but also reporting the “counterintuitive” finding that the Court is less likely to defer to agency views in cases in which the Court applied the two-step *Chevron* framework than in cases in which the Court did not invoke the *Chevron* framework); Merrill, *Judicial Deference*, *supra* note 43, at 982 (using empirical data to show that some cases are still resolved using traditional methods of statutory construction).

66. E.g., *United States v. Boyle*, 469 U.S. 241, 246 n.4 (1985) (deferring to regulation which correlated the statutory “reasonable cause” standard for relief from penalty for late filing of a tax return with “ordinary business care and prudence” as consistent with Congressional intent and over forty years of case law, and citing *Chevron*, 467 U.S. at 844 & n.14). See also *Newark Morning Ledger Co. v. United States*, 113 S. Ct. 1670, 1685-86 (1993) (Souter, J., dissenting) (observing that permitting depreciation for the value of a newspaper’s paid subscribers constitutes a “rejection of statutory interpretation settled by Congress itself through reenactment of the tax code and a further invasion of the political domain to rewrite a Treasury regulation,” and citing pre-*Chevron* cases as well as *Chevron*); *United States v. Burke*, 504 U.S. 229, 242 (1992) (Scalia, J., concurring) (rejecting an

as it has had in other areas of law.⁶⁷ For several years after *Chevron*, the Supreme Court,⁶⁸ commentators,⁶⁹ and the Tax Court⁷⁰ continued to cite pre-*Chevron* authority in discussing whether to defer to agency interpretation of the Code. Commentators suggest several possible reasons for the relative infrequency of citation to *Chevron* in tax cases. Some note that prior to *Chevron*, the Court was already employing a heightened level of deference to administrative interpretations of tax law.⁷¹ Thus, *Chevron* may have been perceived by some as requiring no marked change in approach from prior tax case law on deference. At least one commentator attributes the lack of *Chevron*'s impact on

IRS construction as being outside the "range of reasonable interpretation of statutory text").

67. See Ellen P. Aprill, *Muffled Chevron: Judicial Review of Tax Regulations*, 3 FLA. TAX REV. 51, 54 (1996) (noting that *Chevron* has been mentioned in tax cases only after 1989 and by the Tax Court only since 1992). See generally Sunstein, *Law and Administration*, *supra* note 43, at 2075 ("In an extraordinarily wide range of areas—including the environment, welfare benefits, labor relations, civil rights, energy, food and drugs, banking, and many others—*Chevron* has altered the distribution of national powers among courts, Congress, and administrative agencies.") (footnotes omitted).

68. See, e.g., *Cottage Sav. Ass'n v. Commissioner*, 499 U.S. 554, 560-62 (1991) (citing *National Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979), but not citing *Chevron*).

69. See, e.g., Livingston, *supra* note 2, at 829 n.39 (discussing deference to tax regulations without citing *Chevron*); Zelenak, *supra* note 2, at 673-74 (discussing deference to tax regulations without citing *Chevron*, but instead citing *National Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979)). See also Samuel B. Sterrett, *Suggested Approach for Judicial Interpretation of Regulations That Grant Discretion to Taxpayers*, 12 VA. TAX REV. 477, 494 (1993) (discussing interpretations of regulations without citing *Chevron*, but instead citing *Cottage Sav. Ass'n*, 499 U.S. 554, a post-*Chevron* case that cites pre-*Chevron* authority, including *National Muffler*, in upholding a Treasury regulation).

70. The Tax Court of the United States was established by Congress in 1969 as an Article I court, although its predecessor was an independent agency in the executive branch. See Code § 7441; Pub. L. No. 91-172, § 951, 83 Stat. 730. In one of the first articles discussing *Chevron*'s application to administrative interpretations of tax law, Professor Galler noted that *Chevron* was first cited by the Tax Court in two 1992 decisions, after the Court of Appeals for the Sixth Circuit "gently criticized the Tax Court for its lack of attention to *Chevron*." Linda Galler, *Emerging Standards for Judicial Review of IRS Revenue Rulings*, 72 B.U. L. REV. 841, 844 n.16 (1992) (citing *Peoples Fed. Sav. & Loan Ass'n v. Commissioner*, 948 F.2d 289 (6th Cir. 1991)).

71. Aprill, *supra* note 67, at 57-61 (discussing the "serious" deference standard applied to interpretive tax regulations during the pre-*Chevron* period); Merrill, *Judicial Deference*, *supra* note 43, at 983 n.56 (observing that "even in years when *Chevron* is applied with some frequency [by the Court.] it tends to be invoked less often in areas where there is a particularly rich tradition of pre-*Chevron* precedent on deference," and giving the example of tax cases where "the Court . . . still tends to frame the deference standard in the terms expressed in earlier decisions").

tax law, at least in part, to the insularity of the tax bar.⁷² Just as plausible, however, are the unique characteristics of tax law,⁷³ which arguably entail specialized approaches to interpretation.⁷⁴

The relationship between pre-*Chevron* and post-*Chevron* deference and the effect of *Chevron* on judicial review of administrative interpretations of the tax code raise issues that deserve systematic analysis.⁷⁵ My task here is the more limited one of attempting to parse what the Supreme Court seems to have done in several recent tax cases, and to explore some of the implications for interpretation of

72. Paul L. Caron, *Tax Myopia, Or Mamas Don't Let Your Babies Grow Up to Be Tax Lawyers*, 13 VA. TAX REV. 517, 554-563 (1994) (arguing that the tax bar has neglected *Chevron's* administrative law principles and their proper application).

73. See Livingston, *supra* note 2, at 826-38 (pointing to factors such as the complex and constantly changing nature of the tax code, the contextual style of tax interpretation that emphasizes Treasury regulations, previous judicial determinations and the broader statutory structure rather than the literal meaning of the statute being construed, and the conceptual nature of the tax legislative process, in which House Ways and Means and Senate Finance Committee members do not see the actual statutory language until after the committee report is issued). See also Bradford L. Ferguson et al., *Reexamining the Nature and Role of Tax Legislative History in Light of the Changing Realities of the Process*, 67 TAXES 804 (1989).

74. See John F. Coverdale, *Court Review of Tax Regulations and Revenue Rulings in the Chevron Era*, 64 GEO. WASH. L. REV. 35, 51-73 (1995) (relying on the distinction between legislative and interpretive regulations in the tax context, Congress's provision of independent review of tax determinations, and the pattern of interaction between Congress and the Treasury); Livingston, *supra* note 2, at 872-86. See also Geier, *Textualism*, *supra* note 2, at 462-72 (discussing *Chevron*, and arguing that textualism can lead to incorrect results in tax cases that implicate the structural issues of tax base definition, that is, the notion of what constitutes "income" under an income tax); Zelenak, *supra* note 2, at 636-37 (arguing that nonliteral interpretations of tax law that take into account the structures and policies of the Code are permissible even under "meaning-based," as well as "intent-based" approaches to interpretation).

75. See Aprill, *supra* note 67, at 53 n.10, 55-81 (reporting on results of a study of approximately four hundred lower court tax cases, examining "the extent to which *Chevron* has influenced judicial review of tax regulations"); Coverdale, *supra* note 74, at 53, 60 & n.116 (reporting that in the decade since *Chevron*, appellate and trial courts considered challenges to legislative regulations in at least fifty cases and only fourteen of those cases cited *Chevron*; and of the more than one hundred fifty cases challenging interpretive regulations, only eighteen of the cases mentioned *Chevron*); see also Beverly I. Moran & Daniel M. Schneider, *The Elephant and the Four Blind Men: The Burger Court and Its Federal Tax Decisions*, 39 HOW. L.J. 841, 907-27 (1996) (surveying Burger Court tax opinions that defer to Treasury regulations). The inconsistent application of *Chevron* by the Supreme Court and the corresponding secondary effects on lower courts pose potential empirical and conceptual obstacles to such a comprehensive review of tax cases. For a discussion of some of the difficulties, and their effect on the conclusions reached from the data gathered in a general survey of Supreme Court cases before and after *Chevron*, see Merrill, *Judicial Deference*, *supra* note 43, at 981-82 & n.53 (applying a broad test in deciding whether the Court applied the *Chevron* framework, essentially asking whether the author of the controlling opinion was "thinking about" *Chevron* in setting forth the analysis of deference).

tax statutes. My focus is on the Court's interpretation of Code provisions where the agency's interpretation is provided in the form of a Treasury regulation.⁷⁶ Although revenue rulings⁷⁷ and other forms of

76. For purposes of this inquiry, I do not distinguish between legislative and interpretive regulations in the tax context other than to 1) describe the characteristics of each and 2) point out that both types of Treasury regulations are issued pursuant to notice and comment procedures. See generally Michael Asimow, *Public Participation in the Adoption of Temporary Tax Regulations*, 44 TAX LAW. 343, 350-61 (comparing the administrative law distinction between legislative and interpretive regulations to the distinction applied in tax law, and concluding that "[c]ourts in tax cases should continue to draw the interpretive-legislative line by determining whether the Treasury derived its authority from a specific delegation or from its general rulemaking power under section 7805(a)").

Under the tax law understanding of the distinction, legislative rules are promulgated pursuant to specific statutory authority. E.g., Code §§ 337(d) (providing that the Secretary "shall prescribe such regulations as may be necessary and appropriate" to carry out *General Utilities* repeal, including specific areas of coordination and potential circumvention); 1502 (providing the Secretary with authority to issue consolidated return regulations for affiliated corporations); 7872(c)(1)(E) (providing for application of below market loan rules "[t]o the extent provided in regulations . . . if the interest arrangements of such loan have a significant effect on any Federal tax liability of the lender or the borrower"). Interpretive tax regulations are promulgated pursuant to the more general authority of Code § 7805(a), which provides that "the Secretary shall prescribe all needful rules and regulations for the enforcement of this title . . ." See *Rowan Cos. Inc. v. United States*, 452 U.S. 247, 253 (1981) (discussing the distinction between regulations issued pursuant to general versus specific authority).

Although the Administrative Procedure Act requires agencies to follow notice and comment procedures when promulgating legislative rules, but not interpretive rules, 5 U.S.C. § 553(b)-(d), Treasury customarily follows such procedures with respect to both legislative and interpretive regulations. See MICHAEL I. SALTZMAN, *IRS PRACTICE AND PROCEDURE* ¶ 3.02[3] (2d ed. 1991); Treas. Reg. § 601.601(a)(2), (d)(1) (1996) (requiring notice and comment procedures to be followed as required by the APA and "in such other instances as may be desirable" and providing for the publication of regulations in the *Federal Register* and Code of Federal Regulations).

The Supreme Court cited *Chevron* in upholding the reasonableness of an interpretive regulation promulgated under the authority of Code § 7805(a) in *United States v. Boyle*, 469 U.S. 241, 246 n.4 (1985). See *infra* text accompanying notes 85-93. The relevance of the distinction to whether a regulation is entitled to *Chevron* deference has been a matter of some debate. For extensive discussion of the differences between "specific" and "general" authority regulations in the tax context and the argument that *Chevron* should not apply to tax regulations promulgated under Code § 7805(a), see Coverdale, *supra* note 74. The regulation discussed in Part II would be categorized as "interpretive" or a "general authority" regulation in the tax context.

77. See Treas. Reg. § 601.601(d)(2)(i)(a), (iii) (1996) (defining revenue ruling as an "official interpretation by the Service" that has been issued by the National Office and published in the Internal Revenue Bulletin to "promote correct and uniform application of the tax laws" by the IRS and "to assist taxpayers in attaining maximum voluntary compliance").

interpretative guidance raise related issues,⁷⁸ they also raise format issues⁷⁹ requiring separate analysis.⁸⁰

In general, as discussed below, the Court's deep divisions about the use of legislative history and other tools of statutory construction at step one of the *Chevron* analysis have not had as much impact on tax law because of the Court's general pattern of proceeding quite quickly to a "reasonableness" analysis in tax cases.⁸¹ When step two is reached, there appears to be little difference in the level of deference given by the Court to Treasury regulations during the pre-*Chevron* and post-*Chevron* period.⁸² However, step one of the *Chevron* framework, if applied in a literalist or textualist way, holds potential dangers

78. See generally Manning, *supra* note 49 (distinguishing *Chevron* deference from "the older but closely related principle that an agency's interpretation of its own regulations must receive similar deference" and arguing that the Supreme Court should reject the presumption that the delegation of rulemaking power to an agency gives the agency the right to construe its own rules authoritatively).

79. See *supra* note 61 and accompanying text.

80. See Coverdale, *supra* note 74, at 84-87 (arguing that revenue rulings are entitled to considerably less weight than interpretive regulations); Linda Galler, *Judicial Deference to Revenue Rulings: Reconciling Divergent Standards*, 56 OHIO ST. L. J. 1037, 1040 (1995) (describing emerging and conflicting standards regarding the weight given revenue rulings and arguing that "revenue rulings should be treated consistently in all judicial fora"); Galler, *supra* note 70 (discussing *Chevron* and criticizing *Davis v. United States*, 495 U.S. 472 (1990), in which the Court did not cite *Chevron* but gave "considerable weight" to a revenue ruling providing a contemporaneous and longstanding interpretation of § 170 of the Code, and arguing that courts should not apply *Chevron* deference to revenue rulings); see also Paul L. Caron, *Tax Myopia Meets Tax Hyperopia: The Unproven Case of Increased Judicial Deference to Revenue Rulings*, 57 OHIO ST. L.J. 637 (1996) (critiquing Galler's analysis); Linda Galler, Letter to the Editor, 72 TAX NOTES 769 (Aug. 5, 1996) (replying to Caron's critique).

81. E.g., *United States v. Burke*, 504 U.S. 229, 234 (1992); *Cottage Savings Ass'n v. Commissioner*, 499 U.S. 554 (1991); *United States v. Boyle*, 469 U.S. 241 (1985). See also, e.g., *Commissioner v. Engle*, 464 U.S. 206, 224-27 (1984) (discussing *National Muffler* and refusing to defer to an "unreasonable" interpretation by the Commissioner of a percentage depletion allowance provision); *Commissioner v. Tufts*, 461 U.S. 300, 316-17 (1983) (citing *National Muffler* and deferring to the Commissioner's "reasonable" interpretation of Code §§ 752(c), (d) & § 1001(b), which required the taxpayers to include the full amount of an outstanding nonrecourse obligation in the amount realized on the sale of property); *Rowan Cos. v. United States*, 452 U.S. 247, 253, 262-63 (1981) (holding regulations interpreting the definition of "wages" for employment tax purposes to be unreasonable under the standards of *National Muffler*); see generally James P. Holden & Matthew J. Zinn, *Foreward to Supreme Court Decisions in Taxation: 1983 Term*, 38 TAX LAW. 421, 433-34, Tables 1 and 2 (1985) (listing the Supreme Court's tax deference cases and the voting patterns of the Justices on deference to Treasury regulations).

82. See April, *supra* note 67, at 67 (observing that *National Muffler* places more emphasis on step two of the "reasonableness" inquiry and that the *National Muffler* standard has been applied in tax cases both before and after *Chevron*); Coverdale, *supra* note 74, at 37-38 (arguing that pre-*Chevron* deference standards have been applied by the Court in the tax context).

for tax law because of the importance of construing the Code coherently in light of the overall structure, context, and purpose of tax law.⁸³

The following discussion describes two post-*Chevron* Supreme Court tax decisions that defer to administrative interpretations of tax law. One case cites *Chevron*, and the other does not, although in both cases the Court applied a two-step type analysis.⁸⁴ These cases are discussed in some detail to show how the Court approached its interpretive task.

The year after *Chevron* was decided, the Court cited *Chevron* in *United States v. Boyle*.⁸⁵ In *Boyle*, the Court deferred to a regulation interpreting Code section 6651(a)(1),⁸⁶ and held that a taxpayer's reliance on an attorney to prepare and file an estate tax return did not constitute "reasonable cause" so as to defeat a statutory penalty incurred because of late filing.⁸⁷ The Court first noted that the term "reasonable cause" is not defined in the Code.⁸⁸ The relevant Treas-

83. *E.g.*, Livingston, *supra* note 2; Zelenak, *supra* note 2. Applied in a textualist form, step one of the *Chevron* analysis would preclude consideration of the legislative history and purpose of the specific tax provision being interpreted, its prior interpretation, and how the provision relates to the policy and structure of the tax code as a whole. *See* Geier, *Textualism*, *supra* note 2.

84. The extent to which the analysis used by the Court resembles *Chevron* is subject to debate. Professor Coverdale states in a recent article that the Supreme Court has never applied *Chevron* deference to interpretive tax regulations. Coverdale, *supra* note 74, at 59 (acknowledging that the "failure to grant *Chevron* deference to general authority regulations in the handful of cases in which it might have done so could indicate that the Court considers *Chevron* inapplicable to general authority regulations" or it may "reflect nothing more than the confused state of its deference jurisprudence."); *but see* David A. Brennan, *Treasury Regulations and Judicial Deference in the Post-Chevron Era*, 13 GA. ST. L. REV. 387, 417 (1997) (concluding that although the Court has not cited *Chevron* with any frequency in tax cases, *Chevron* deference is "alive and well with respect to Treasury regulations"). My reading of the cases suggests that the Court's discussion is consistent with a *Chevron*-type two step framework, with a more searching emphasis on the reasonableness inquiry at step two. I differ with Professor Coverdale with regard to what the Court seems to be doing at step one, in which the Court quickly notes the silence or ambiguity of the statute with regard to the question at issue, but agree that the Court's "step two" analysis lists factors more closely identified with a less deferential standard or a more searching reasonableness inquiry than was applied in *Chevron*. Our disagreement may thus simply center on the extent to which the Court's analysis in tax cases resembled a two-step approach rather than whether the Court has applied *Chevron* in the tax area in the same highly deferential way it has been applied in other contexts.

85. 469 U.S. 241, 246 n.4 (1985).

86. *Id.* To escape the late filing penalty, the taxpayer had to prove under § 6651(a)(1) that the failure did not result from "willful neglect," and that the failure was due to "reasonable cause." *Id.* at 245.

87. *Id.* at 252.

88. *Id.* at 246.

ury Regulation requires the taxpayer to show that, despite "ordinary business care and prudence," the taxpayer is "unable to file the return within the prescribed time."⁸⁹ The taxpayer argued unsuccessfully that the statute applies a standard of willfulness only, and that the regulation is incompatible with the statute because it converts the statute into a test of "ordinary business care."⁹⁰ After examining various amendments to the statutory provision and noting the lack of any legislative history discussing the change in language,⁹¹ the Court concluded that Congress intended to require the "absence of fault":

A taxpayer seeking a refund must therefore prove that his failure to file on time was the result neither of carelessness, reckless indifference, nor intentional failure. Thus, the Service's correlation of "reasonable cause" with "ordinary business care and prudence" is consistent with Congress' intent, and over 40 years of case law as well. That interpretation merits deference. *See, e.g., Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844, and n.14 (1984).⁹²

The Court thus deferred to the regulation's interpretation of "reasonable cause" and applied a "bright line" approach, holding that reliance by the executor on an attorney (as the executor's agent) to file the return did not relieve the executor (as principal) of the duty to file a timely return.⁹³

The Court relied on pre-*Chevron* authority six years after *Boyle* in *Cottage Savings Ass'n v. Commissioner*.⁹⁴ Without citing *Chevron*,

89: *Id.* (citing 26 C.F.R. § 301.6651(c)(1)(1984)).

90: *Id.* at 246 n.4.

91: *Id.* at 245 n.3.

92: *Id.* at 246 n.4. The specific page from *Chevron* cited by the Court in *Boyle* includes the following discussion of implicit delegation:

Sometimes the legislative delegation to an agency on a particular question is implicit rather than explicit. In such a case, a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency. . . . We have long recognized that considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer, and the principle of deference to administrative interpretations "has been consistently followed by this Court whenever decision as to the meaning or reach of a statute has involved reconciling conflicting policies, and a full understanding of the force of the statutory policy in the given situation has depended upon more than ordinary knowledge respecting the matters subjected to agency regulations."

467 U.S. at 844 (footnotes and citations omitted).

The Court's cite to *Chevron* is thus somewhat ambiguous. The Court may be either (i) applying *Chevron* deference to Treasury's interpretive regulation or (ii) citing *Chevron* for its discussion of pre-*Chevron* deference.

93: *Boyle*, 469 U.S. at 251-52.

94: 499 U.S. 554 (1991).

the Court applied a *Chevron*-type framework, but cited pre-*Chevron* case law in applying the deference standard. *Cottage Savings* involved the simultaneous sale and repurchase by a savings and loan association of participation interests in different pools of home mortgage loans secured by single-family houses.⁹⁵ Under then existing Federal Home Loan Bank Board (FHLBB) accounting rules,⁹⁶ the mortgages were treated as having been exchanged for “substantially identical” ones held by other lenders.⁹⁷ As a result, the transactions were not reported as losses for FHLBB purposes.⁹⁸ When *Cottage Savings* claimed a \$2.44 million tax loss on the sale of the mortgages, the Internal Revenue Service disallowed the deduction.⁹⁹

The Service claimed that no loss had been “realized” on the “sale or other disposition of property” under section 1001(a) of the Code.¹⁰⁰ According to the Service, no “disposition” had occurred because the properties exchanged were not “materially different,” as required under the applicable Treasury regulation.¹⁰¹ The savings association claimed that any exchange of property constituted a “disposition of property” under section 1001(a), regardless of whether the property exchanged was “materially different.”¹⁰² Alternatively, the association argued that the participation interests were “materially different” because the underlying loans were secured by different properties.¹⁰³

The Court first noted that “[n]either the language nor the history of the Code indicates whether and to what extent the property exchanged must differ” to be a “disposition” under section 1001(a).¹⁰⁴ The Court then deferred to the “material difference” interpretation of the Treasury regulation, citing a pre-*Chevron* case for the deference standard:

Because Congress has delegated to the Commissioner the power to promulgate “all needful rules and regulations for the enforcement of [the Internal Revenue Code],” 26 U.S.C. § 7805, we must defer to his regulatory interpretations of the Code so long as they are rea-

95. *Id.* at 557-58.

96. The Court noted that the FHLBB rules had been relaxed to facilitate transactions that would generate tax losses without affecting the economic position of the savings and loan associations. *Id.* at 557.

97. *Id.*

98. *Id.* at 558.

99. *Id.*

100. *Id.* at 559.

101. *Id.* at 559-60 (discussing Treas. Reg. § 1.1001-1).

102. *Id.* at 560.

103. *Id.*

104. *Id.*

sonable, see *National Muffler Dealers Ass'n, Inc. v. United States*, 440 U.S. 472, 476-77.¹⁰⁵

After examining the history of the longstanding regulation, which had remained unchanged through various Code reenactments, and its consistency with the Court's landmark cases on realization, the Court found the regulation's interpretation of section 1001(a) to be "reasonable."¹⁰⁶

The Court in *Cottage Savings* thus appeared to rely on the pre-*Chevron* deference standard at step two of its analysis, when it determined that the agency's interpretation of section 1001(a) was "reasonable." Although the Court found the "material difference" standard to be a "reasonable" interpretation of the statute, it refused to apply the standard in the way suggested by the Service and held that the tax loss was realized when properties with "legally distinct entitlements" were exchanged.¹⁰⁷

In *National Muffler*,¹⁰⁸ the pre-*Chevron* case cited by the Court in *Cottage Savings*, the Court had first noted the statutory term at issue, "business league,"¹⁰⁹ was "so general" that an interpretive regulation was appropriate.¹¹⁰ The Court explained that in such a situation it customarily defers to the regulations "found to 'implement the congressional mandate in some reasonable manner.'"¹¹¹ The Court noted that deference to the Treasury regulation was appropriate because Congress delegated to the Secretary of the Treasury and his delegate, the Commissioner of Internal Revenue, the task of prescribing rules and regulations for the enforcement of the Code.¹¹² That delegation

105. *Id.* at 560-61.

106. *Id.* at 561-66.

107. *Id.* at 566. The Court declined to defer to the Service's application of the regulation to the facts of the case because the Service had not issued "an authoritative, prelitigation interpretation" of what property exchanges satisfy the "material difference" requirement. *Id.* at 562-63. The Court instead examined the case law and structure of the Code provision from which the test derived and concluded that the properties were "materially different" because the exchanged interests embodied "legally distinct entitlements." *Id.* at 566. The Court concluded that the loss was therefore "realized" under § 1001(a) when the properties were exchanged. *Id.*

108. *National Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979).

109. The Court in *National Muffler* held that a trade association that confined its membership to Midas muffler dealers and their concerns was not entitled to tax exempt status as a "business league" within the meaning of Code § 501(c)(6). *Id.* at 488-89.

110. *Id.* at 476.

111. *Id.* at 476-77 (citing *United States v. Cartwright*, 411 U.S. 546, 550 (1973) (quoting *United States v. Correll*, 389 U.S. 299, 307 (1967))).

112. *Id.* at 477 (citing Code § 7805(a)).

helps ensure consistency in application and best utilizes agency expertise.¹¹³

The Court then articulated the following test in its review of agency interpretation:

In determining whether a particular regulation carries out the congressional mandate in a proper manner, we look to see whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose. A regulation may have particular force if it is a substantially contemporaneous construction of the statute by those presumed to have been aware of congressional intent. If the regulation dates from a later period, the manner in which it evolved merits inquiry. Other relevant considerations are the length of time the regulation has been in effect, the reliance placed on it, the consistency of the Commissioner's interpretation, and the degree of scrutiny Congress has devoted to the regulation during subsequent re-enactments of the statute.¹¹⁴

The Court observed that the Commissioner's interpretation of the Code provision at issue, while not the only possible one, "bear[s] a fair relationship to the language of the statute, it reflects the views of those who sought its enactment, and it matches the purpose they articulated."¹¹⁵ In addition, the regulation evolved over fifty years to "reflect congressional design" and had been "infrequently but consistently" interpreted by the agency.¹¹⁶

Both pre-*Chevron* and post-*Chevron* authority suggest that if the Code provision being construed is silent or ambiguous, the Court will defer to a "reasonable" interpretation of the statute by the agency. As noted above, a Treasury regulation will be found "reasonable" under *National Muffler* if it "harmonizes with the plain meaning of the statute, its origin, and its purpose."¹¹⁷ Before reaching the "reasonableness" step of the analysis under *Chevron*, however, the Court considers whether the deference standard is triggered under step one.¹¹⁸

The relationship between the *Chevron* framework and the gloss on "reasonableness" provided by *National Muffler* is problematic. If the Court takes a textualist approach to the question of the statute's meaning at step one, it may not reach the step two "reasonableness" inquiry. If step two is reached, it is unclear how the Court would ap-

113. *Id.*

114. *Id.* (footnotes omitted).

115. *Id.* at 484.

116. *Id.*

117. *Id.* at 477.

118. *See supra* text accompanying notes 52-60.

ply *National Muffler*, which requires that the regulation harmonize with the statute's origin, purpose, and "plain meaning."

Professor Ellen Aprill has suggested that the *National Muffler* approach to judicial review of tax regulations provides a model for revising the application of the *Chevron* doctrine in contexts beyond tax.¹¹⁹ Under the revised formulation, which Aprill calls the "muffled" *Chevron* approach, the Court would begin by examining the plain meaning of the statute, looking to its language and structure but not its legislative history. However, unlike the textualist's application of the *Chevron* step one, the first step of the reformulated *Chevron* approach, according to Aprill, would not presume that the statute's meaning is plain. Under Aprill's approach, plain meaning would be "the exception rather than the rule."¹²⁰ In step two, the reviewing court judges the reasonableness of administrative interpretation against the origin and purpose of the statute, particularly as shown in the legislative history.

Although Professor Aprill's proposal for "muffling" *Chevron* offers a practical way of blunting the effects of *Chevron* on lower court review of agency action once step two is reached,¹²¹ it does not suggest a basis for countering what Professor Aprill identifies as Supreme Court "practice" of presuming that the meaning of a statute is plain. Without such a basis, it is unclear why the Court should depart from current practice or why a reformulated textual analysis would result in a finding of plain meaning less often than now occurs.¹²²

119. Aprill, *supra* note 67, at 55, 81-90.

120. *Id.* at 82. It is unclear from Professor Aprill's discussion, which focused more on step two of the analysis, how this standard would apply in practice. She cites an article discussing the Tax Court's evolving approach to plain meaning for "factors that the Tax Court has required before finding that language is plain." *Id.* at 82 n.185 (citing Ilyse Barkan, *New Challenges to Use of the Plain Meaning Rule to Construe the IRC and Regs*, 69 TAX NOTES 1403 (Dec. 11, 1995)). The factors discussed in the cited Barkan article (the absurdity, consistency, futility, and omissions tests), however, do not appear to represent a significant departure from the textualist methodology.

121. Professor Aprill's "muffled *Chevron*" proposal is drawn in part from the Tax Court's application of *Chevron* and *National Muffler*:

[T]ax opinions often transform the *National Muffler* tripartite test of harmony with the plain language of the statute, its origin, and its purpose into a two-step test. The first step looks at the statutory language. The second step considers purpose and origin through the use of legislative history. These two steps differ in important ways from both the original *Chevron* two-step and the two-step as reformulated by Justice Scalia. This "muffled *Chevron* doctrine"—a combination of *National Muffler* and *Chevron*—offers a model for statutory interpretation and regulatory review applicable beyond tax.

See Aprill, *supra* note 67, at 81-82.

122. *Id.* at 88-90.

Professor John Coverdale, on the other hand, proposes collapsing steps one and two into a pre-*Chevron* type analysis in which there would be no need for a default presumption of administrative interpretative primacy in cases of statutory gaps or ambiguities.¹²³ Unlike Aprill's proposal, his approach completely rejects the application of the *Chevron* two-step analysis in the tax context, but allows courts to take the agency views into account even as the judges retain their pre-*Chevron* authority to be the ultimate arbiters of a statute's meaning and scope.

As discussed below, the relative respite that tax law has enjoyed from the plain meaning approach may be in the process of ending. The Supreme Court may in the future more frequently resolve tax cases at step one by applying a plain meaning analysis. If that development occurs, the results may turn on whether or not the statute can be found to have a "plain meaning" rather than on whether Treasury's interpretation of the Code is reasonable.

II. A Case Study: Inconsistency About Ambiguity and the Resulting Doctrinal Incoherence of *Burke, Schleier*, and *O'Gilvie*

Three times in the last five years, the Supreme Court has interpreted the scope of section 104(a)(2) of the Code. In two cases, the Court decided whether the exclusion from gross income for amounts received "on account of personal injuries"¹²⁴ encompasses certain em-

123. See Coverdale, *supra* note 74, at 89. Under this approach, a *National Muffler* analysis would apply in challenges to interpretive tax regulations, with the courts acting as primary interpreters of the Code and giving significant weight to the agency's views. *Id.* at 67. Thus, rather than applying a two-step analysis, in which courts must accept any minimally reasonable agency view when Congress has not spoken directly to the issue, courts would instead weigh the agency's views along with its own interpretation of the statute. *Id.* at 89. For legislative tax regulations, courts would accept any reasonable position of the agency (as *Chevron* would require at step two) but "they should take the agency's views into account in their initial reading of the statute, rather than ignoring the agency until after they have determined whether Congress has spoken to the issue addressed in the regulation." *Id.* This proposal generally calls for adoption of a position articulated by commentators prior to *Chevron*, in which the standard of judicial review of agency interpretation would reflect the substantive content of the agency action being reviewed. *Id.* at 35 (citing Ernest Gellhorn & Glen O. Robinson, *Perspectives on Administrative Law*, 75 COLUM. L. REV. 771, 783 (1975)).

124. For the text of the statute applied by the Court in these cases, see *supra* note 27. As discussed in Part III, Congress amended § 104(a)(2) last summer so that the exclusion from gross income is now limited to any damages (other than punitive damages) received on account of personal physical injuries or physical sickness. See *infra* note 232.

ployment discrimination recoveries. In *United States v. Burke*¹²⁵ and in *Commissioner v. Schleier*,¹²⁶ the Court acknowledged that under certain circumstances employment discrimination could constitute a "personal injury" within the meaning of the statute, but held that the particular sex and age-based discrimination recoveries received by the taxpayers were not excludable from gross income. In December 1996, in *O'Gilvie v. United States*,¹²⁷ the Court held that punitive damages received for physical personal injuries were not excludable from gross income.

Although the three decisions each rejected the taxpayers' claims, the Court applied quite different interpretive approaches. Unlike the general pattern of deference in the tax cases discussed in the previous part, *Schleier* provides an example of a tax case in which the Court did not rely upon the "reasonableness" of Treasury's interpretation of the statute, but instead relied primarily upon the Code's "plain meaning."¹²⁸ In contrast, three years before *Schleier*, the Court in *Burke* appeared to view the same Code provision as ambiguous and to accept at the outset of its analysis the Treasury regulation, which identifies personal injuries as those based upon tort or tort-type rights.¹²⁹ In *O'Gilvie*, the Court applied the rationale of *Schleier* to a physical injury case, but at the same time acknowledged the linguistic ambiguity of the "plain" language interpreted by the Court in *Schleier*.¹³⁰

The different approaches taken by the Court in these three cases provoke at least two questions. First, did the Court's different inter-

125. 504 U.S. 229, 242 (1992) (holding that settlement of Title VII back pay claims for sex-based wage discrimination are not amounts received "on account of personal injuries" excludable under Code § 104(a)(2)).

126. 115 S. Ct. 2159, 2164-65 (1995) (holding that back pay and liquidated damages under ADEA are not amounts received "on account of personal injuries" under Code § 104(a)(2)).

127. 117 S. Ct. 452 (1996) (holding that punitive damages award of \$10 million received in a tort suit by the husband and two children of a woman who died of toxic shock syndrome was not excludable from gross income under Code § 104(a)(2) because it was not received "on account" of personal injuries).

128. See 115 S. Ct. at 2164-65. See also *United States v. Brockamp*, 117 S. Ct. 849, 851-52 (1997) (Breyer, J.) (holding in a unanimous decision that the statutory limitations period provided by 26 U.S.C. § 6511 for tax refund claims does not authorize equitable tolling); *Commissioner v. Lundy*, 116 S. Ct. 647 (1996) (O'Connor, J.) (applying a "plain meaning" interpretation of 26 U.S.C. § 6512(b)(3)(B), which provides a "look back" period for obtaining a refund of overpaid taxes in the U.S. Tax Court). Justice O'Connor was joined in the majority in *Lundy* by Chief Justice Rehnquist and Justices Scalia, Kennedy, Souter, Ginsburg, and Breyer. Justice Stevens dissented, and also joined the dissenting opinion of Justice Thomas.

129. *Burke*, 504 U.S. at 234.

130. *O'Gilvie*, 117 S. Ct. at 454-55.

pretive approaches result in different conclusions about the meaning of section 104(a)(2), or can the cases be reconciled? Second, if the Court did reach different conclusions about the meaning of a statutory term in these cases, what are the implications of the Court's struggle with its interpretive task?

As argued in this part, two of the cases give inconsistent meanings to the same statutory provision excluding from "gross income" the "amount of any damages received . . . on account of personal injuries or sickness."¹³¹ In *Burke*, the Court accepted without qualification the regulation's interpretation of the scope of the statute.¹³² In *Schleier*, the Court relied on a plain meaning analysis of the text of the statute and found the Treasury regulation's tort-type rights standard to be either limited in its ambit or in addition to the statutory requirement that the amounts be received "on account of personal injuries."¹³³ At bottom, the Court's two views about the scope and plain meaning of the Code cannot be reconciled. In addition, the Court's contradictory conclusions about the statute's ambiguity in *Burke*, *Schleier*, and *O'Gilvie* signify that the Court's doctrines of statutory interpretation are dangerously manipulable. The inconsistent approaches led the Court into a doctrinal tangle.

The discussion below first briefly summarizes the interpretive approaches and holdings in *Burke* and *Schleier*, describes the two-part test articulated by the Court in *Schleier*, and then examines the two components of the test in some detail. It ends with a discussion of how the co-existing parts of the test create confusion about what constitutes a "personal injury," and how *O'Gilvie* dealt with some related interpretive issues in the quite different context of punitive damages received for physical personal injuries.

In *Burke*,¹³⁴ the Court held that amounts paid in settlement of sex-based wage discrimination claims under Title VII of the Civil

131. Code § 104(a)(2).

132. See *Burke*, 504 U.S. at 234.

133. 115 S. Ct. at 2166. In rejecting the taxpayer's reliance on the regulation, the Court stated that "[w]e need not decide whether the Commissioner would have authority to dispense entirely with the statutory requirement, because she disclaims any intent to do so, and the text of the regulation does not belie her disclaimer." *Id.*

134. The *Burke* case was filed as a tax refund suit by three women employees of the Tennessee Valley Authority (TVA). *Burke v. United States*, 90-1 U.S. Tax Cas. (CCH) ¶ 50,203 (E.D. Tenn. 1990), *rev'd*, 929 F.2d 1119 (6th Cir. 1991), *rev'd*, 504 U.S. 229 (1992). The women received distributions under the settlement of a Title VII action brought against the TVA by an individual plaintiff and the Office and Professional Employees International Union (the "Union"). 90-1 U.S. Tax Cas. (CCH) ¶ 50,203 at 83,744-45. Under the settlement agreement, the TVA agreed to pay \$4,200 to the original individual plaintiff

Rights Act of 1964 are not “damages . . . received on account of personal injuries,” and thus are not excludable from gross income under section 104(a)(2).¹³⁵ Although the majority opinion¹³⁶ does not cite or discuss *Chevron*, the Court appears to apply something like the *Chevron* framework.¹³⁷ It concludes that neither the text nor legislative history provides any explanation of the term “personal injuries,” and then it relies on a Treasury regulation that interprets the Code section.¹³⁸ The majority opinion refers to the “tort or tort type rights” standard of the regulations under section 104(a)(2),¹³⁹ and explains that “IRS regulations formally have linked identification of a personal injury for purposes of section 104(a)(2) to traditional tort principles.”¹⁴⁰ Although Justice Scalia’s concurring opinion rejects the regulation’s tort type rights standard as an unreasonable interpretation of

and a total of \$5 million to the other affected employees. *Id.* at 83,746. The TVA withheld federal income taxes and social security taxes from amounts distributed to claimants receiving an allocated portion of the \$5 million settlement award. *Id.* at 83,746-47. Several of the claimants then filed for refund of the withheld taxes, asserting that the § 104(a)(2) exclusion was applicable to a Title VII settlement award. *Id.* at 83,747.

The district court denied the refund claim, ruling that, because the women had sought and obtained back pay rather than compensatory or other damages, the amounts were not excludable as damages for personal injuries. *Id.* at 83,749. The Sixth Circuit reversed, holding that the exclusion under § 104(a)(2) depended upon whether the injury and the claim were “personal and tort-like in nature,” 929 F.2d at 1121, 1124, and concluding that Title VII provided a tort-like cause of action for injury to the dignity of the person. *Id.* at 1121-22. The Supreme Court reversed the judgment of the Court of Appeals, relying on Title VII’s remedial scheme to hold that the injury and claim were not tort-like in nature. *Burke*, 504 U.S. at 237-242.

135. *Burke*, 504 U.S. at 242.

136. Justice Blackmun wrote the majority opinion, joined by Chief Justice Rehnquist and Justices White, Stevens, and Kennedy. Justices Scalia and Souter wrote concurring opinions. Justice O’Connor wrote a dissenting opinion, which was joined by Justice Thomas.

137. The validity of the regulation itself was not at issue in *Burke*. Both the government and the taxpayer relied on the regulation for the applicable “tort or tort type rights” standard, but disagreed about its application in cases where the damages were measured by loss of income. *See infra* note 143; *cf.* Merrill, *Textualism*, *supra* note 58, at 376-77 (categorizing the *Burke* case in the Appendix entitled “Agency Deference Cases in the Supreme Court 1991-92 Terms” as accepting the agency interpretation, but not following the *Chevron* framework and thus not applying a step two analysis).

138. 504 U.S. at 234.

139. Treas. Reg. § 1.104-1(c) (1996). The full text of the regulation is set forth below:
 (c) *Damages received on account of personal injuries or sickness.* Section 104(a)(2) excludes from gross income the amount of any damages received (whether by suit or agreement) on account of personal injuries or sickness. The term “damages received (whether by suit or agreement)” means an amount received (other than workmen’s compensation) through prosecution of a legal suit or action based upon tort or tort type rights, or through a settlement agreement entered into in lieu of such prosecution.

140. *Id.* at 234.

the statute,¹⁴¹ the other eight Justices accept the regulation's interpretation¹⁴² of the statutory exclusion's scope.¹⁴³

In *Schleier*,¹⁴⁴ the Court held that back pay and liquidated damages in settlement of an age discrimination claim were not excludable

141. Justice Scalia first explains in *Burke* that a "commonsense" construction of the terms "personal injuries or sickness" in § 104(a)(2) would limit application of the exclusion to injuries to the recipients' physical or mental health, and thus, the exclusion ought not apply to nonphysical injuries such as defamation. *Id.* at 243-44 (Scalia, J., concurring). Significantly, he acknowledges that his "commonsense" reading of the statute is inconsistent with the "tort rights" formulation adopted by the Treasury regulation. *Id.* at 245-46. Citing the *Chevron* case, he rejects the regulatory standard as "not within the range of reasonable interpretation of the statutory text." *Id.* at 242. He concedes that the term "personal injuries" could be read in isolation to encompass noncontractual injuries for which remedies would be provided in an action for damages. *Id.* at 242-43. Nevertheless, because the term is part of the phrase "personal injuries and sickness," he concludes that the words should not be interpreted beyond their "more narrow and normal meaning" as referring to injury to the body of the person. *Id.* at 243. Applying the canon of statutory construction "noscitur a sociis" and examining the use of the phrase "personal injuries and sickness" in other subsections of § 104(a), he concludes that "personal injuries" refer only to physical or mental health injuries. *Id.* at 243-44 (translating the maxim "noscitur a sociis" as meaning "a word is known by the company it keeps").

Under his statutory analysis, the settlement payments are not "on account" of personal injuries within the meaning of § 104(a)(2). *Id.* at 245 (Scalia, J., concurring). Although he concedes that a victim of employment discrimination could suffer psychological harm, he emphasizes that the "entitlement to back pay under Title VII does not depend on such a showing." *Id.* In his view, the only redressable legal injuries under Title VII are produced by "economic deprivation." *Id.* Thus, he concludes that settlement amounts in respect of back pay do not come within the statutory exclusion. *Id.*

142. The dissent in *Burke* agrees that the Court properly deferred to the tort type rights standard of the regulations, citing a pre-*Chevron* case, *United States v. Correll*, 389 U.S. 299 (1967). *Burke*, 504 U.S. at 249 (O'Connor, J., dissenting). The *Correll* case is cited in both the post-*Chevron* case of *Cottage Savings*, 499 U.S. 554, 561 (1991), and the pre-*Chevron* case, *National Muffler*, 440 U.S. 472, 477 (1979).

143. The *Burke* opinions diverge, however, when the Justices apply the regulation's standard to the taxpayer's Title VII claims. The concurring opinion by Justice Souter acknowledges good reasons in favor of placing Title VII on either side of the line dividing contract and tort actions. *Id.* at 247-48 (Souter, J., concurring). Turning to a "default rule" of statutory interpretation—that exclusions from income must be narrowly construed—he concludes that he need not decide whether the action was more "tort-like" or more "contract-like." *Id.* at 248. In his view, where application of the exclusion is not clear, the exclusion of income should be denied. *Id.* The dissenting opinion by Justice O'Connor disagrees with the majority's focus on the range of remedies available as a means of determining whether the claim was "tort-like" in nature, and would more broadly apply the "nature of the claim" analysis. *Id.* at 248-54 (O'Connor, J., dissenting, joined by Thomas, J.).

144. 115 S. Ct. 2159 (1995). The *Schleier* case arose from the settlement of a class action ADEA suit brought by former United Airlines employees, including pilots and other flight crew members, who were automatically terminated at age sixty. *Id.* at 2161-62. The former employees won a jury verdict of willful violation of ADEA by United. *Id.* at 2162. The District Court's judgment in favor of the employees was reversed on appeal due to erroneous jury instructions. *Monroe v. United Air Lines*, 736 F.2d 394 (7th Cir. 1984),

from gross income under section 104(a)(2).¹⁴⁵ In an opinion by Justice Stevens,¹⁴⁶ the majority concluded that no part of the settlement is excludable under the plain meaning of the statutory requirement that the damages be received on account of personal injuries.¹⁴⁷ In addition, the majority concluded that recoveries under the Age Discrimination in Employment Act (ADEA)¹⁴⁸ are not based upon "tort or tort type rights."¹⁴⁹

The *Schleier* case articulates "two independent requirements" that must be met before a recovery may be excluded from gross income under section 104(a)(2).¹⁵⁰ First, the underlying claim giving rise to recovery must be based on "tort or tort type rights."¹⁵¹ Second, the damages must be received "on account of personal injuries or sickness."¹⁵² The first requirement derives from the Court's opinion in *Burke* and the text of the applicable regulation.¹⁵³ The second requirement is set forth by the Court for the first time in *Schleier*, and it

cert. denied, 470 U.S. 1004 (1985). The parties then reached a settlement under which United agreed to pay each class action plaintiff a specific amount designated as back pay and liquidated damages in equal proportions. 115 S. Ct. at 2162. United withheld income taxes from back pay portion but not the liquidated damages portion of the settlement payments. *Id.*

Under the settlement agreement, Erich Schleier received \$145,629. *Id.* When he filed his 1986 federal income tax return, he included the back pay portion in income but excluded the portion attributed to liquidated damages. *Id.* After the Service issued a deficiency notice asserting that the liquidated damages portion should have been included in gross income, Schleier filed a Tax Court petition claiming that he had correctly excluded the liquidated damages. *Id.* He also sought a refund for the tax he had paid on the back pay portion of the settlement. *Id.* In an unreported opinion, the Tax Court agreed with Schleier, concluding that the entire settlement amount was excludable from gross income under § 104(a)(2). *Id.* The Fifth Circuit affirmed without opinion, relying on a prior panel decision that had applied the tort-like standard adopted in *Burke* and found age discrimination awards to be excludable. *Id.* at 2162-63. The Supreme Court granted review to resolve a conflict among the Courts of Appeal concerning "the taxability of ADEA recoveries in general and of the United settlement in particular." 115 S. Ct. at 2163.

145. 115 S. Ct. at 2167.

146. Justice Stevens' majority opinion was joined by Chief Justice Rehnquist, and Justices Kennedy, Ginsburg, and Breyer. Justice Scalia concurred in the judgment without authoring or joining an opinion. Justice O'Connor dissented, joined by Justice Thomas and in part by Justice Souter. Thus, in both *Burke* and *Schleier*, only five Justices comprised the majority, with three of the same Justices in the majority each time. *See supra* note 136.

147. 115 S. Ct. at 2165.

148. 29 U.S.C. § 626(b).

149. 115 S. Ct. at 2167.

150. *Id.*

151. *Id.*

152. *Id.*

153. *Id.* at 2165-67 (referring to Treas. Reg. § 1.104-1(c) (1996)). For the text of the regulation, *see supra* note 139.

is based on the language of the statute itself.¹⁵⁴ The inconsistencies between the two parts of the test can best be understood by examining in detail what the Court says about each requirement—beginning with the approach adopted in *Burke*.

A. The Tort or Tort Type Rights Standard: Determining the Nature of the Claim

In *Burke*, the Court applied the “tort or tort type rights” standard of the regulations to determine whether the sex discrimination claim asserted was in the nature of a personal injury claim.¹⁵⁵ The Court examined the remedial scheme of the employment discrimination statute to determine whether the claim asserted was sufficiently tort-like.¹⁵⁶ The majority reasoned that Title VII in its then applicable form¹⁵⁷ did not redress tort type rights because it did not permit recovery for traditional harms associated with personal injury such as pain and suffering, emotional distress, harm to reputation, and other consequential damages.¹⁵⁸ Title VII permitted only the award of back pay, injunctions, and other equitable relief.¹⁵⁹ The original Title VII

154. *Id.* at 2164-65. The statutory language also is repeated in the text of the regulations. See *supra* notes 27 & 139.

155. 504 U.S. 229, 237 (1992). Prior to *Burke*, the government had extensively litigated the issue of attempted exclusions from gross income for intangible personal injuries. For a discussion of pre-*Burke* cases, see, e.g., J. Martin Burke & Michael K. Friel, *Tax Treatment of Employment-Related Personal Injury Awards: The Need for Limits*, 50 MONT. L. REV. 13 (1989) and Mary L. Heen, *An Alternative Approach to the Taxation of Employment Discrimination Recoveries Under Federal Civil Rights Statutes: Income from Human Capital, Realization, and Nonrecognition*, 72 N.C. L. REV. 549, 583-92 (1994). The government's position had evolved over a period of more than seventy years, from one in which only physical injuries were encompassed by the statute to its position in *Burke* that the “focus of the inquiry is whether the nature of the recovery for a claim of nonphysical injury compensates for a personal loss or represents an economic gain.” Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit at 10 n.7, *United States v. Burke*, 504 U.S. 229 (1992) (No. 91-42). For intangible injuries, the Service thus relied on a distinction between recoveries for “personal” injuries as opposed to “business” or economic injuries.

The Supreme Court in *Burke* adopted the “nature of the claim” test, holding that employment discrimination could constitute a “personal injury” within the meaning of § 104(a)(2) “if the relevant cause of action evidenced a tort-like conception of injury and remedy.” 504 U.S. at 237, 239.

156. *Id.* at 237 n.7.

157. The Court in *Burke* applied the law in effect prior to the Civil Rights Act of 1991, Pub. L. 102-166, 105 Stat. 1071, which amended Title VII's remedial scheme to include compensatory and punitive damages for certain claims of intentional discrimination. 504 U.S. at 237-38 n.8.

158. *Id.* at 239.

159. See *id.* at 238.

remedial scheme thus did not “recompense a Title VII plaintiff for any of the other traditional harms associated with personal injury.”¹⁶⁰

The Court acknowledged that employment discrimination or other injury to nonphysical personal interests constitutes a “personal injury” for purposes of federal tax law if the relevant cause of action “evidenced a tort-like conception of injury and remedy.”¹⁶¹ However, the majority distinguished Title VII from other federal antidiscrimination statutes with more expansive remedial schemes.¹⁶² The Court focused on the limited nature of the back pay remedy, stating that “Congress declined to recompense Title VII plaintiffs for anything beyond the wages properly due them—wages that, if paid in the ordinary course, would have been fully taxable.”¹⁶³ Accordingly, the Court held that Title VII does not redress a tort-like personal injury within the meaning of section 104(a)(2) and applicable regulations.¹⁶⁴

The *Schleier* opinion subsequently clarified two aspects of the “tort or tort type rights” standard adopted in *Burke*. First, the Court emphasized that the primary characteristic of an action based on tort type rights is the availability of compensatory remedies.¹⁶⁵ The taxpayer had argued that the availability of a jury trial and liquidated damages in age discrimination actions brought such claims within the *Burke* test.¹⁶⁶ The Court held that those features were not sufficient, stating that the ADEA provided no compensation for many traditional harms associated with personal injury.¹⁶⁷ The Court concluded that monetary recoveries were limited to back wages, which are of an

160. *Id.* at 239.

161. *Id.*

162. The Court distinguished Title VII from 42 U.S.C. § 1981 and fair housing actions under Title VIII of the Civil Rights Act of 1968, which both allow for jury trials and for compensatory and punitive damages. *See id.* at 240.

163. *Id.* at 241 (citation omitted).

164. Under the amendments provided in the Civil Rights Act of 1991, claims of intentional discrimination may be tried before a jury and remedied with compensatory and punitive damages. The taxpayers in *Burke* argued that the expanded scope of Title VII, as amended, provided additional support for their contention that Title VII claims are inherently tort-like in nature. The Court rejected that argument, but, at the same time, suggested that it might reach a different result under the amended version of the statute, and noted that “Congress’ decision to permit jury trials and compensatory and punitive damages under the amended Act signals a marked change in its conception of the injury redressable by Title VII.” *Id.* at 241 n.12. The Court concluded, however, that the amendments could not be imported back into analysis of the statute as it existed at the time of the taxpayer’s lawsuit against their employer. *See id.*

165. 115 S. Ct. at 2166.

166. *See id.*

167. *See id.* at 2167.

“economic character,”¹⁶⁸ and that liquidated damages serve a punitive rather than a compensatory function.¹⁶⁹ While observing that “this is a closer case than *Burke*,” the Court concluded that a claim under the ADEA “is not one that is ‘based upon tort or tort type rights.’”¹⁷⁰

Second, the Court held that satisfaction of the “tort or tort type” standard is a necessary, but not sufficient, condition for excludability under section 104(a)(2).¹⁷¹ Although the Court acknowledged in a footnote that a post-*Burke* revenue ruling¹⁷² suggested that satisfac-

168. *See id.*

169. Schleier had argued that ADEA liquidated damages served to compensate victims of discrimination for personal injuries that are difficult to quantify. *See id.* at 2164. The Court agreed that if Congress had intended ADEA’s liquidated damages to compensate plaintiffs for personal injuries, those damages might come within the exclusion. *See id.* at 2165. The Court saw two weaknesses in Schleier’s argument, however. First, even if Congress were aware of an earlier decision which had described liquidated damages under the Fair Labor Standards Act as compensating for “obscure” injuries, Congress may not have understood that observation “as referring to injuries that were personal rather than economic.” *Id.* Second, the Court emphasized that it had previously concluded that ADEA liquidated damages were a departure from those in the Fair Labor Standards Act, and were intended by Congress to be punitive in nature. *See id.* (citing *Trans World Airlines v. Thurston*, 469 U.S. 111, 125 (1985)). Thus, the Court held that the liquidated damages described by ADEA are not received “on account of personal injury or sickness.” *Id.*

The *Schleier* decision thus pointed toward resolution of the issue of punitive damages because of its resolution of the liquidated damages issue. The Court viewed ADEA liquidated damages to be punitive rather than compensatory, and held that they were not damages received “on account of personal injuries or sickness.” *Id.* *But cf.* Robert W. Wood, *Schleier Strikes Taxpayers Three Times*, 68 TAX NOTES 475, 478-79 (July 24, 1995) (stating that although “the Supreme Court has tipped its hand that punitive damages may not be excludable in any circumstance,” there “are certainly arguments that punitives in true personal injury cases (such as the hypothetical automobile accident case described by the Supreme Court) should be excludable from income”).

170. 115 S. Ct. at 2167.

171. *See id.*

172. Rev. Rul. 93-88, 1993-2 C.B. 61. The ruling applied the nature of the claim test adopted in *Burke* to employment discrimination remedies available to claimants under Title VII, 42 U.S.C. § 2000(e) (1988), the Americans With Disabilities Act, 42 U.S.C. §§ 12101-12213 (Supp. III 1991), and 42 U.S.C. § 1981 (1994) (prohibiting racial discrimination in “making, performance, modification, and termination of contracts, and the enjoyment of all benefits, privileges, terms, and conditions of the contractual relationship”). The Service examined the range of remedies available for each theory of recovery available under each statute. If the specific claim asserted involved “tort or tort type rights,” all of the amounts received were excluded. Under that approach, the Service held that compensatory damages and back pay received for Title VII disparate treatment sex discrimination claims were excludable under § 104(a)(2). The Service explained that the same result would apply even if the recovery in the case were limited to back pay. Back pay received for disparate impact sex discrimination, however, would not be excludable. In addition, the Service held that compensatory damages and back pay received in satisfaction of a claim for racial discrimination under 42 U.S.C. § 1981 and Title VII are excludable under § 104(a)(2). The Service specified that the same result would be reached if the intentional race discrimination recoveries were limited to back pay. Under the reasoning of the ruling,

tion of the "tort type rights" standard is sufficient, the Court observed that "the Service's interpretive rulings do not have the force and effect of regulations" and "may not be used to overturn the plain meaning of a statute."¹⁷³

B. Amounts Received "On Account of Personal Injuries": The Statutory Standard

The Court's "plain meaning" reading of section 104(a)(2) provides the basis of the Court's newly articulated separate and independent requirement for excludability. Without citing *Chevron* or discussing the two-step analysis, the Court began with an illustration of "the usual meaning of 'on account of personal injuries'" by examining a "typical recovery in a personal injury case" such as an automobile accident.¹⁷⁴ If the hypothetical injured taxpayer suffered medical expenses, lost wages, pain and suffering and emotional distress, and settled the resulting lawsuit for \$30,000, the entire amount is excludable under section 104(a)(2). According to the Court, "each element of the settlement is recoverable not simply because the taxpayer received a tort settlement, but rather because each element of the settlement satisfies the requirement set forth in 104(a)(2) . . . that the damages were received 'on account of personal injuries or sickness.'"¹⁷⁵

The Court then compared its accident hypothetical with an age discrimination settlement. Although at "first glance" the back pay award may appear comparable to the accident victim's recovery of lost wages, the Court rather cryptically concluded that a back pay award is different: "Whether one treats respondent's attaining the age of 60 or his being laid off on account of his age as the proximate cause of respondent's loss of income, neither the birthday nor the discharge can fairly be described as a 'personal injury' or 'sickness.'"¹⁷⁶ Although the Court acknowledged that an "unlawful termination may

recoveries in cases with both disparate treatment and disparate impact claims would be partially excludable and partially taxable, raising potentially difficult allocation issues. The ruling took no position on age discrimination recoveries or the taxation of punitive damages.

After *Schleier*, the Service revoked the ruling and asked for public comment on how its position should be revised in light of the Supreme Court's decision in *Schleier*. Notice 95-45, 1995-34 I.R.B. 20. In the meantime, in situations affected by *Schleier*, the Service would not issue letter rulings on whether amounts received are excludable from gross income under § 104(a)(2). Rev. Proc. 96-3, §§ 1.02, 5.05, 1996-1 I.R.B. 82.

173. 115 S. Ct. at 2167 n.8 (citations omitted).

174. *Id.* at 2163.

175. *Id.* at 2164.

176. *Id.*

have caused some psychological or 'personal' injury comparable to the intangible pain and suffering caused by an automobile accident," the Court concluded "it is clear that no part of respondent's recovery of back wages is attributable to that injury."¹⁷⁷

The Court emphasized that in the hypothetical automobile accident, the accident causes a personal injury which causes a loss of wages.¹⁷⁸ In contrast, "[i]n age discrimination, the discrimination causes both personal injury and loss of wages, but neither is linked to the other."¹⁷⁹ Thus, the Court concluded that the back pay is not excludable under section 104(a)(2) because an ADEA back pay recovery is not received "'on account of' any personal injury and because no personal injury affected the amount of back wages recovered."¹⁸⁰

The dissenting opinion by Justice O'Connor¹⁸¹ pointed out the implicit contradiction between the *Burke* and *Schleier* understanding of what is meant by damages received on account of a "personal injury."

Justice O'Connor argued in the first part of her opinion, joined by Justice Thomas, that the majority's analysis contradicted its fundamental premise that "personal injury" can encompass both tangible and intangible harms.¹⁸² The hypothetical contrast between ADEA back pay and lost wages as a result of an accident has significance, Justice O'Connor asserted, "only if one presumes that there is a relevant difference for purposes of section 104(a)(2) between the car crash and the illegal discrimination."¹⁸³ Although physical and mental injuries "differ from the economic and stigmatic harms that discrimination inflicts upon its victims," the difference has no relevance for purposes of section 104(a)(2) unless the Court were distinguishing between tangible and intangible harms.¹⁸⁴ Justice O'Connor then compared ADEA injuries to the harm to reputation and loss of business income caused by defamation. The injuries "may not always manifest themselves in physical symptoms, but they are no less personal," and should be excluded under section 104(a)(2).¹⁸⁵

177. *Id.*

178. *See id.*

179. *Id.*

180. *Id.*

181. *See id.* (O'Connor, J., dissenting).

182. *See id.* at 2167-68.

183. *Id.* at 2169.

184. *Id.*

185. *Id.* at 2169-70. The defamation example chosen by Justice O'Connor was significant because of the nature of the claim analysis adopted by *Burke*, which implicitly re-

In the second part of her opinion, joined by Justices Thomas and Souter, Justice O'Connor argued that notwithstanding that "fundamental defect" in the Court's analysis, ADEA damages should be excluded under the test established in *Burke*.¹⁸⁶ She also took issue with the imposition of an independent statutory requirement.¹⁸⁷ She pointed out that for thirty-five years the Service had interpreted its regulation as establishing the overall ambit of section 104(a)(2), and specifically as establishing the meaning of the term "personal injuries." That was also the position taken by the Service in *Burke*, in a post-*Burke* revenue ruling, and presented by the government to the courts below and in their opening brief before the Court in *Schleier*. According to Justice O'Connor, only the Commissioner's reply brief contradicted that long history.¹⁸⁸ She argued that unless the Court was willing to find the Service's longstanding prior position unreasonable, the prior interpretations and practices of the Service could not be ignored.¹⁸⁹

Responding to the majority's position that agency rules may not be used to "overturn the plain meaning of a statute," she insisted that

jected the pre-*Burke* litigation position taken by the Service in defamation and malicious prosecution cases. *See supra* note 155.

186. Justice O'Connor pointed out that the Court in *Burke* deferred to the regulation, stating that "discrimination could constitute a 'personal injury' for purposes of § 104(a)(2) if the relevant cause of action evidenced a tort-like conception of injury and remedy." *Id.* at 2170 (O'Connor, J., dissenting) (quoting *Burke*, 504 U.S. at 239). Unlike Title VII, ADEA provides for jury trials and does not limit relief to back pay. ADEA "authorizes courts to grant the panoply of 'such legal or equitable relief as will effectuate the purposes' of the Act." *Id.* (emphasis in original). Regardless of whether liquidated damages are classified as compensatory or punitive, the remedies available under ADEA go beyond the circumscribed remedies permitted under Title VII. According to the dissenters, those distinctions qualified an ADEA suit as a tort-type action under *Burke*. *See id.*

187. *See id.* at 2171.

188. *See id.* *See supra* discussion of format issues at text and notes 61 & 79-80. Justice Stevens quoted the government's reply brief as arguing that the regulation authorizes the application of the exclusion "only when it both (i) was received through prosecution or settlement of an 'action based upon tort or tort type rights' . . . and (ii) was received 'on account of personal injuries or sickness.'" *Id.* at 2166. The government's reply brief provided the following example to illustrate that the definition in Treas. Reg. § 1.104-1(c) of the regulations could not be understood apart from the statutory requirement:

[A] corporation or individual may recover damages under a "tort or tort type" cause of action—such as claims for injuries to property, fraud, and trade libel—that would not qualify for an exclusion from income under the statute because they involve injuries to property or other economic interests rather than injuries to the person.

See Reply Brief for the Petitioner at n.2, Commissioner v. Schleier, 115 S. Ct. 2159 (1995) (No. 94-500).

189. *See* 115 S. Ct. at 2171 (O'Connor, J., dissenting).

the "language of the statute is anything but plain."¹⁹⁰ The regulation was promulgated to deal with the ambiguity of the concept of "personal injuries," which had resulted in controversies over the scope of the exclusion. Rather than declare the regulation to be unreasonable, the majority merely added a statutory requirement without being clear "where besides the definition of personal injury there is room in the statute for the agency to graft on this additional requirement."¹⁹¹ It would be much more reasonable, Justice O'Connor concluded, to read the regulation as defining an ambiguous statutory phrase than to create a superfluous statutory requirement.¹⁹²

C. The Co-existing Standards Created New Confusion About What Constitutes a "Personal Injury"

The Court's decision in *Schleier* is quite difficult to parse without reading it as a shift away from the *Burke* Court's interpretation of "personal injuries," which tests the nature of the discrimination claim by looking to whether the underlying cause of action evidences a tort-like conception of injury and remedy. *Schleier* introduces a requirement that employment discrimination may not in itself constitute a "personal injury" if the compensatory amounts received for violation of the civil rights statutes are measured by economic loss.

The reasoning of the two cases cannot be reconciled even under the *Schleier* majority's view that it was interpreting an independent requirement. Under the Court's explanation of the two "independent" requirements, the Court accepted *Burke's* view of the meaning "personal injury" as provided by the regulation but then went on to interpret the statutory requirement that the damages received be "on account of a personal injury." The problem with the Court's view of what it did in *Schleier* is that although the "independent" statutory requirement may have separate content for noncompensatory recoveries, it does not have such content for compensatory recoveries.

As explained earlier, *Burke* applied the nature of the claim test by considering whether the discrimination claims asserted constituted tort-type rights. After *Burke*, the lower courts addressed the issue of whether the discrimination recoveries were "personal injury" recoveries by considering whether the remedial scheme of the antidiscrimination statute at issue provided traditional tort or tort type

190. *Id.* at 2172.

191. *Id.*

192. *Id.*

remedies.¹⁹³ Once it had been determined that the underlying claim was tort-like in nature, it was assumed that compensatory recoveries were received "on account" of the personal injury.¹⁹⁴

That assumption by the lower courts was grounded in the language of the statute. The terms "any damages received . . . on account of personal injuries" could mean either 1) *any* damages received in personal injury actions, or 2) any damages received *as compensation for* personal injuries.¹⁹⁵ Under the former meaning, all damages received in personal injury litigation would be excludable regardless of whether or not they are compensatory.¹⁹⁶ Under the latter meaning, amounts received for noncompensatory reasons would not come within the statutory exclusion. For example, punitive damages may serve purposes such as punishment or deterrence and thus arguably are not received "on account" of personal injuries under the second meaning.¹⁹⁷ Similarly, pre- or post-judgment interest on recovery amounts may be received to compensate for the lost time value of money, not to compensate for personal injuries, and thus arguably are

193. For a discussion of post-*Burke* lower court decisions, see Heen, *supra* note 155, at 598-606.

194. *Id.* See also *supra* note 172 (discussing Rev. Rul. 93-88).

195. See Mary Jane Morrison, *Getting a Rule Right and Writing a Wrong Rule: The IRS Demands a Return on All Punitive Damages*, 17 CONN. L. REV. 39, 58-61 (1984).

196. For articulation of such a view based on the "plain meaning" of § 104(a)(2), see Debra Cohen-Whelan, *From Injury to Income: The Taxation of Punitive Damages "on Account of" United States v. Schleier*, 71 NOTRE DAME L. REV. 913 (1996).

197. Post-*Burke* analysis of the excludability of punitive damages was mixed. Several post-*Burke* lower court decisions considered the question of whether punitive damages are received "on account" of personal injuries, and reached conflicting conclusions. The post-*Burke* cases finding punitive damages to be taxable pointed out that punitive damages are not received "on account" of the injury, but are designed to punish or discourage certain behavior. See, e.g., *Estate of Moore v. Commissioner*, 53 F.3d 712, 713 (5th Cir. 1995); *Wesson v. United States*, 48 F.3d 894, 896 (5th Cir. 1995); *Hawkins v. United States*, 30 F.3d 1077, 1084 (9th Cir. 1994), *cert. denied*, 115 S. Ct. 648 (1994); *Reese v. United States*, 24 F.3d 228, 235 (Fed. Cir. 1994); *Commissioner v. Miller*, 914 F.2d 586, 589-90 (4th Cir. 1990), *on remand*, T.C. Memo. 1993-49 (allocating the proceeds between compensatory and punitive damages), *aff'd per curiam*, 60 F.3d 823 (1995). Those cases finding punitive damages to be excludable from income relied on dictum in *Burke* and the Court's nature of the claim analysis. *Burke*, 504 U.S. at 236 n.6 (stating that, in 1989, "Congress amended § 104(a) to allow the exclusion of *punitive* damages only in cases involving 'physical injury or physical sickness.'). According to those cases, if a claim involved a "personal injury," any type of damages received, including punitive damages, would be excludable. See, e.g., *Horton v. Commissioner*, 33 F.3d 625, 625-26 (6th Cir. 1994), *aff'g* 100 T.C. 93 (1993). The Supreme Court granted review of one of those cases and issued its decision in December 1996. See *O'Gilvie v. United States*, 92-2 U.S. Tax Cas. (CCH) ¶ 50,567 (D. Kan. 1992) (holding excludable in punitive damage award and modifying pre-*Burke* ruling of taxability on motion for reconsideration in light of Supreme Court's decision in *Burke*), *rev'd*, 66 F.3d 1550 (10th Cir. 1995), *cert. granted*, 116 S. Ct. 1316 (1996), *aff'd*, 117 S. Ct. 452 (1996).

not received "on account" of personal injuries.¹⁹⁸ In contrast, compensatory personal injury recoveries, such as amounts for pain and suffering, emotional distress or medical costs, would be excludable. The "on account of" language of the statute thus establishes an independent restriction only with regard to noncompensatory recoveries. Without acknowledging the above ambiguity with respect to the meaning of the statutory terms "any damages . . . received on account of personal injuries," the *Schleier* majority applied the latter meaning based on a "plain meaning" analysis.¹⁹⁹

By contrast, in *O'Gilvie*,²⁰⁰ the Court explicitly acknowledged the statutory ambiguity.²⁰¹ In an opinion by Justice Breyer,²⁰² the majority noted first that "the phrase 'on account of' does not unambiguously define itself."²⁰³ The Court then construed the provision as encompassing only compensatory damages, noting that such an interpretation would be more consistent with the dictionary definition, with the Court's prior decision in *Schleier*, and with the statute's history and the tax-related purpose of excluding compensatory damages

198. Morrison, *supra* note 195, at 55-57; see *Brabson v. United States*, 73 F.3d 1040, 1047 (10th Cir. 1996) (holding that statutory prejudgment interest awarded in a personal injury action was not received "on account" of personal injury within meaning of § 104(a)(2) because it is compensation for the lost time value of money, not compensation for the personal injury); *Kovacs v. Commissioner*, 100 T.C. 124, 130 (1993) (concluding that interest on wrongful death damages is not excludable under § 104(a)(2)), *aff'd*, 25 F.3d 1048 (6th Cir. 1994).

199. See Part II.B. *supra*.

200. 117 S. Ct. 452 (1996). In *O'Gilvie*, the husband and two children of a woman who died of toxic shock syndrome paid federal income taxes on a jury award of \$10 million punitive damages (but not on the \$1.525 million in actual damages received) in a tort suit against the maker of the product that caused the decedent's death. They then filed refund claims. The government refunded the income taxes paid by the children and later filed suit to recover the refund. The husband's refund suit and the government's suit against the children were filed in the same District Court, which found for the taxpayers in each case on the ground that the statutory exclusion from gross income includes punitive damages. The Tenth Circuit reversed, and the Supreme Court granted certiorari to resolve the conflict in the circuits on this issue. See *supra* note 197.

201. See *id.* at 454 (pointing out two possible linguistic interpretations of the phrase "on account of" as (1) "a 'but for' connection between 'any' damages and a lawsuit for personal injuries," or (2) requiring a "stronger causal connection, making the provision applicable only to those personal injury lawsuit damages that were awarded by reason of, or because of, the personal injuries," that is, as compensation for the injury rather than to punish the tortfeasor's conduct).

202. Justice Breyer's majority opinion was joined by Chief Justice Rehnquist, and Justices Stevens, Kennedy, Souter, and Ginsburg. Justice Scalia dissented, joined by Justices O'Connor and Thomas. For a discussion of Justice Breyer's likely impact on the development of administrative law, see Richard J. Pierce, Jr., *Justice Breyer: Intentionalist, Pragmatist, and Empiricist*, 8 ADMIN. L. J. AM. U. 747 (1995).

203. 117 S. Ct. at 454.

that, "making up for a loss, seek to make a victim whole, or, speaking very loosely, 'return the victim's personal or financial capital.'"²⁰⁴ Thus, in *O'Gilvie*, the Court agreed with the *Schleier* conclusion, but only after recognizing the linguistic ambiguity of the statute and applying a contextual analysis, which construed the words in light of the statute's legislative history and tax-related purpose.²⁰⁵

Significantly, the *Schleier* Court treated the statutory "on account of" test as independent of the tort or tort-type rights standard without explaining how the two can be independent for compensatory recoveries. As noted above, recoveries to compensate for a discrimination claim found to be tort-like in nature were presumed prior to *Schleier* to be received "on account of personal injuries." *Schleier* rejected that approach, although it remained unclear where the Court would draw the line between damages received on account of a "personal" versus an "economic" injury.²⁰⁶

204. *Id.* at 456 (citing H.R. REP. NO. 767, at 9-10 (1918)).

205. In his dissenting opinion, Justice Scalia applied a textual analysis, and argued that the "ordinary meaning" of the statute would encompass the exclusion of both compensatory and punitive damages. See *O'Gilvie* 117 S. Ct. at 460 (Scalia, J., dissenting). Justice Scalia criticized the majority for proceeding "too quickly from its erroneous premise of ambiguity to analysis of the history and policy behind section 104(a)(2)." *Id.* at 460. In addition, Justice Scalia disagreed with the majority's view that the result in *O'Gilvie* was foreshadowed by the Court's decision in *Schleier*. He emphasized that as the "dissent accurately observed [in *Schleier*], 'the key to the Court's analysis' was the determination that an ADEA cause of action did not necessarily entail 'personal injury or sickness,' so that the damages awarded for that cause of action could hardly be awarded 'on account of personal injuries or sickness.'" *Id.* at 462 (citations omitted).

206. For example, consider two different types of claims, defamation and Title VII sexual harassment claims, where the claims arguably are tort or tort type in nature. For the defamation claim, if the injury involved damage to professional reputation as opposed to personal reputation, the question of whether the lost past or future income would be excludable or not depends upon an interpretation of the term "personal injury." The *Schleier* decision suggests that if the injury is "personal," lost pay would be excluded under § 104(a)(2) if the requisite link between the injury and the recovery exists. It is unclear, however, whether the lost pay would be viewed as received "on account" of an injury that is "personal" as opposed to "economic" in nature. At the very least, the question could have been raised again after *Schleier*, despite a string of pre-*Burke* litigation losses for the government on this very issue.

Sexual harassment claims raise similar issues. A sexual harassment violation under Title VII, as amended in 1991, may be remedied by back pay and other equitable relief, and under certain circumstances, by compensatory and punitive damages. See 42 U.S.C. §§ 2000(e)-5(g), 1981a (a), (b) (Supp. III 1991); *Meritor Sav. Bank, FSB v. Vinson*, 477 U.S. 57, 66-67 (1986). Assuming that a Title VII sexual harassment claim would be held to be a tort-type claim, lower courts would also be faced with deciding whether any back pay received is "on account" of "personal injuries." The answer would not be clear under *Schleier*. Lower courts would have to determine whether the "personal injury" caused by sexual harassment should be viewed as being compensated for by amounts received for back pay as well as for emotional distress, pain and suffering, and medical reimbursements.

In conclusion, *Schleier* added an undefined statutory limitation which precluded the exclusion from gross income of back pay recoveries in the employment discrimination setting but did not preclude the exclusion of recoveries for lost wages or lost earning capacity in the physical injury setting.²⁰⁷ That limitation conflicted with its earlier decision in *Burke*.²⁰⁸ The Court therefore created new uncertainty about what constituted a "personal injury" within the meaning of section 104(a)(2).²⁰⁹

III. Implications for Tax Law: Normative Issues

The cases discussed in Part II give cause for concern about the impact of the Court's evolving approach to statutory interpretation on

Arguably, under *Schleier*, the personal injury caused by sexual harassment would be confined to personal humiliation or loss of personal dignity, and not the "economic" injury of lost pay. On the other hand, the loss of pay caused by a sexually hostile working environment seems very similar to the loss of pay caused by a physical personal injury to a worker. The humiliation and related dignitary injuries may themselves be viewed as causing the loss of pay. Under that analysis, back pay should be viewed as being received "on account" of a "personal injury" within the meaning of § 104(a)(2).

As these examples suggest, the Court gave new undefined content to the term "personal injuries" in *Schleier*. Although the Court rejected an explicit distinction between tangible and intangible harm in *Burke* and *Schleier*, it may have adopted an implicit rule based on the distinction between economic and noneconomic harms, which would have led to significant allocation and other difficulties in administering the exclusion. See generally F. Philip Manns, Jr., *Down and Out: RIFed Employees, Taxes, and Employment Discrimination Claims After Burke and Schleier*, 44 U. KAN. L. REV. 103, 123-33 (1995).

207. The "on account of" language would have separate content for back pay only if the Court refused to view back pay as damages received in compensation for the "personal injury" of employment discrimination. Such a narrow technical view of the term "damages" (as limited to compensatory legal damages and not applicable to equitable relief, see *Sparrow v. Commissioner*, 949 F.2d 434 (D.C. Cir. 1991), *cert. denied*, 112 S. Ct. 3009 (1992)) was arguably rejected in *Burke*, 504 U.S. at 237. For a discussion of the compensatory nature of back pay awards, see Heen, *supra* note 155, at 572-74.

208. Rather than correct the problems created by its earlier decision in *Burke*, the Court grafted another independent requirement onto the problematic "tort or tort type" standard. As a result, although the Court may have been seeking to resolve some of the issues generated by *Burke's* adoption of the "tort or tort type" standard, it resurrected other issues put to rest in *Burke*. See *supra* note 155. For a discussion of some of these issues, see, e.g., Heen, *supra* note 155, at 598-606; Douglas A. Kahn, *Compensatory and Punitive Damages for a Personal Injury: To Tax or Not to Tax?*, 2 FLA. TAX REV. 327 (1995). See also Arthur W. Andrews, *The Taxation of Title VII Victims After the Civil Rights Act of 1991*, 46 TAX LAW. 755 (1993); Leandra Lederman Gassenheimer, *The Excludability of Employment Discrimination Awards under Code Section 104(a)(2) after Burke v. United States and Commissioner v. Schleier*, 28 ARIZ. ST. L.J. 315 (1996); Bernard Wolfman, *Current Issues of Federal Tax Policy*, 16 U. ARK. LITTLE ROCK L.J. 543, 547-51 (1994).

209. See generally, *Leading Cases*, 109 HARV. L. REV. 111, 319-29 (1995) (discussing the lack of coherent analysis in *Schleier*).

the development of tax law. A majority of the Court in *Schleier* applied a “plain meaning” approach to section 104(a)(2) when it had declined to do so only three years before. The opinion was not written by a textualist, but by Justice Stevens. When read in light of the implications of the Court’s ruling in *Burke*, it is difficult to reconcile it with deference principles or with the Court’s earlier interpretation of the same statutory terms in *Burke*. However, in *O’Gilvie*, in an opinion written by Justice Breyer and joined by Justice Stevens, the Court applied a contextual analysis of the “on account of” language in section 104(a)(2), reinforcing the conceptual inconsistency between the two “independent” tests applied in *Schleier*.

As discussed in Part II, the problems generated by these cases have their origin in the Court’s inconsistent interpretive approaches and the resulting adoption and then marginalization of the standard articulated in the Treasury regulation. Perhaps *Burke*, *Schleier*, and *O’Gilvie* are best viewed as small pieces of a larger and quite difficult puzzle, in which the Court’s struggle to reach a consensus on interpretive issues has interfered with a coherent resolution of the underlying substantive problem. As suggested by these cases, an inconsistent emphasis on the “plain meaning” of the Code could create piecemeal and incoherent interpretations.

Nevertheless, even if the “plain meaning” approach were more consistently applied by the Court, problems related to the inherent limitations of the approach would remain. The Court’s application of the plain meaning approach often restricts its use of potentially illuminating contextual information. Applied in a textualist form, the plain meaning approach generally precludes consideration of the legislative history and purpose of the specific tax provision being interpreted, its prior interpretation, and its relationship to the policy and structure of the tax code as a whole. Although the Court’s debate about its interpretive approach in statutory construction and administrative agency deference cases has not had as much impact on tax law for the reasons discussed in Part I, there is evidence that the Court’s approach in tax cases is beginning to reflect its more general reliance on “plain meaning.” An increased emphasis on “plain meaning” analysis of the Code poses an increased risk of misinterpretation in tax cases.

Because both the plain meaning approach and *Chevron* deference apply only if the statutory provision is unambiguous, much depends upon the Court’s conclusion about ambiguity. The Court’s reluctance to find statutory ambiguity could itself lead to increased doctrinal incoherence. As *Schleier* illustrates, the Court sometimes

fails to recognize or to acknowledge statutory ambiguity. Without an acknowledgement of ambiguity, the Court may interpret statutory language without reference to prior administrative interpretations, creating a double danger. Without reference to contextual information and without deference to administrative interpretation, more frequent plain meaning analysis may lead to an increase in incoherent and unpredictable results, making effective tax administration more difficult.

A more consistent and complete immersion in the history and purpose of section 104(a)(2) might have led to a more coherent interpretive result,²¹⁰ but would it have been worth the effort? Would it lead to a better decision-making approach over the long term? Is Professor Schauer correct in suggesting that the plain meaning approach represents better use of judicial resources?²¹¹ Why should the Court engage in the more time-consuming task of becoming expert in the history and policy of the Code in general and the specific provision being interpreted in particular if the plain meaning approach arguably offers a more efficient and normatively beneficial decision-making procedure?

In raising these types of questions, and suggesting that they be answered in favor of the plain meaning approach, Professor Schauer focuses quite specifically on the function of plain meaning as a decision-making procedure independent of "any conception of the primacy of one governmental body rather than another as a matter of political theory."²¹² Although this decision-making function, and the

210. Professor Schauer argues that one way of evaluating the "plain meaning" approach as compared to a more contextual form of decision-making is to compare the frequency of interpretive "mistakes" over a large number of cases. See Schauer, *Practice and Problems*, *supra* note 3, at 740-41. Whether a more far-ranging contextual analysis of § 104(a)(2) by the Court would have resulted in a more coherent result has been debated. Compare Geier, *Textualism*, *supra* note 2, at 472 (concluding that consideration of the structure and policy of the Code would not have led to a better decision in this context); with Heen, *supra* note 155, at 554-55 (concluding that such consideration would have led to a better result). In undertaking an analysis of the frequency of the Court's mistakes, it is questionable whether commentators would consistently agree on whether a "mistake" has been made, or even if they so agreed, whether they would reach the same conclusion about the nature of the Court's "mistake."

211. According to Professor Schauer, that approach may have particular advantages in tax cases:

My instinct is that these Justices with these clerks with this amount of time will make less of a hash of tax law in the long run by trying to rely on plain meaning than by trying to divine and apply the deepest purposes and equities of the Internal Revenue Code. And even if I am wrong about this, it would not surprise me if the Justices themselves thought this.

Schauer, *Coordinating Function*, *supra* note 12, at 254 n.85.

212. Schauer, *Practice and Problems*, *supra* note 3, at 731.

institutional stability it may promote, could plausibly explain the increased use of plain meaning analysis, it would not justify its use in the tax context. Whether such a decision-making procedure should be used by the Court in interpreting the Code requires consideration of the roles played by the various governmental branches in the development of tax law.²¹³

The risk of incoherent results has a direct effect on efforts to administer the tax laws in a uniform and consistent way. How can such mistakes or inconsistencies be minimized in interpretation of the tax laws? As mentioned above, there are a range of possibilities. The Court could immerse itself in the details and complexities of the Code, utilizing a wide range of sources of meaning, and reach its best answer to interpretive questions given the statutory language, purpose, history and context. Alternatively, the Court could defer to reasonable interpretations of the Code by Treasury, to the extent that Congress has delegated the agency such responsibility. Finally, as suggested by Professor Schauer's analysis, the Court could use a suboptimal "second best" plain meaning approach to interpretation as a resource-saving mechanism and let Congress fix its mistakes. If those were the choices, the Court should opt for the first or second approach rather than the third. Either would be preferable to what Professor Schauer identifies as the resource-conserving plain meaning approach. My own preference would be for the Court to apply a contextually informed interpretation of the Code, which would permit consideration of Treasury's views, among other factors, and to apply a heightened deference standard only where Congress has explicitly delegated legislative-type authority to Treasury.²¹⁴

The following sections discuss normative issues raised by reliance on the plain meaning approach, including an evaluation of the costs of relying on legislative correction and the benefits of protecting the public from captured administrative agencies. I conclude that there are legitimate reasons in the tax context to reject the plain meaning approach as a resource-saving decision-making procedure.

213. Professor Schauer acknowledges that the determination of when the plain meaning approach is desirable as a form of decisionmaking is "necessarily domain-contextual," and states that "the degree to which comparatively acontextual interpretive approaches in the service of some diminution of agency power would be desirable will vary as well." *Id.* at 736-37.

214. For a persuasive discussion of these issues, see Coverdale, *supra* note 74, at 67-79, 88-89.

A. Legislative Correction

Increased reliance on legislative correction raises issues of legislative resource allocation and of comity. It is not easy to get Congress to fix interpretive mistakes of reviewing courts—at least not readily enough to ameliorate the tax administration burdens resulting from suboptimal and possibly inconsistent decisions. Legislative correction becomes even more difficult if the legislative fix were to result in revenue losses rather than revenue gains.²¹⁵ Although it may not be as difficult for Congress to fix courts' tax interpretation mistakes²¹⁶ as it may be in other areas of the law²¹⁷ in which legislative activity occurs less frequently, the resource allocation issues posed by such reliance on legislative correction still raise legitimate concerns.²¹⁸ On the whole, comity among the branches of government will be better served if courts try to make sense of the statutory provision in light of its context, recognizing that congressional correction may be delayed or may not occur at all if congressional action cannot be galvanized.²¹⁹

Consider for example the seven-year period prior to the adoption by Congress of amendments to section 104(a)(2) in 1996. Congress first considered a legislative answer to the question of the excludability of employment discrimination recoveries when it adopted amendments to the Code in 1989.²²⁰ Although the House passed a bill that would have restricted the exclusion to physical injuries,²²¹ there was

215. See Geier, *Purpose*, *supra* note 2, at 511 n.62. *But cf.* Zelinsky, *supra* note 2, at 729 (“The need for legislative repair is classically perceived when the literal application of the Code leads to a pro-taxpayer result that is unacceptable to Treasury officials, Congress’s tax-writers, and the professionals who advise them.”).

216. See Zelinsky, *supra* note 2, at 728-29 (arguing that the Code is highly correctable by legislation).

217. For a discussion of the reasons why legislative correction of the Court’s interpretation of a specific provision enacted as part of a larger piece of legislation may be difficult to achieve, see *Johnson v. Transportation Agency*, 480 U.S. 616, 671-72 (1987) (Scalia, J., dissenting).

218. See James J. Brudney, *Congressional Commentary on Judicial Interpretations of Statutes: Idle Chatter or Telling Response*, 93 MICH. L. REV. 1, 20-32, 38 (1994) (discussing the opportunity costs and other resource issues involved in legislative correction).

219. See *id.* at 87-89. See also, e.g., William N. Eskridge, Jr., *Overriding Supreme Court Statutory Interpretation Decisions*, 101 YALE L.J. 331 (1991); Abner J. Mikva & Jeff Bleich, *When Congress Overrules the Court*, 79 CAL. L. REV. 729 (1991); John Copeland Nagle, *Corrections Day*, 43 UCLA L. REV. 1267, 1280-90 (1996).

220. Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, 103 Stat. 2106 (1989) [hereinafter OBRA ‘89].

221. H.R. 3299, 101st Cong., 1st Sess., pt. 2 § 11641 (1989). The House Report observed that courts have interpreted the § 104(a)(2) exclusion “broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness. For example, some courts have held that the exclusion applies to damages in cases involving

no corresponding Senate provision and the conference committee did not adopt the House proposal.²²² Without explanation of its action, the conference committee instead adopted an entirely different amendment limiting the exclusion for certain punitive damages received in cases involving nonphysical injuries.²²³ Three years and many lower court decisions later,²²⁴ the Supreme Court interpreted the unamended version of the statute in *Burke*. Litigation over the application of the statute to nonphysical injuries continued after *Burke* and *Schleier*. In 1995, after *Schleier*, the House passed an amendment to section 104(a)(2) similar to its 1989 provision.²²⁵ This time, the conference committee adopted the House amendment, as modified by the Senate.²²⁶ President Clinton vetoed the provision as part of a massive omnibus budget reconciliation bill.²²⁷ In 1996, the House passed another provision similar to its 1989 proposal.²²⁸ The Senate bill contained no parallel provision, although it did contain a

employment discrimination and injury to reputation where there is no physical injury or sickness." H.R. Rep. No. 247, 101st Cong., 1st Sess. 1354-55, *reprinted in* 1989 U.S.C.C.A.N. 1906, 2824-25.

222. H.R. Conf. Rep. No. 386, 101st Cong., 1st Sess., *reprinted in* 1989 U.S.C.C.A.N. 3018.

223. The 1989 Act inserted at the end of § 104(a)(2) the sentence "[p]aragraph (2) shall not apply to any punitive damages in connection with a case not involving physical injury or physical sickness." OBRA '89, *supra* note 220, § 7641(a), 103 Stat. at 2379 (amending Code § 104(a)(2) (1988)).

The OBRA amendment did not apply to the punitive damage award in *O'Gilvie*. The taxpayers argued in *O'Gilvie*, however, that in 1989 Congress must have assumed that punitive damages received for physical injuries would remain excludable. The Court suggested that the OBRA language may merely have reflected an awareness that the law was unclear for both physical and nonphysical injuries, and that Congress "wanted to clarify the matter in respect to nonphysical injuries, but it wanted to leave the law where it found it in respect to physical injuries." 117 S. Ct. at 457. In any event, the Court refused to rely on the views of a later Congress in interpreting an earlier statute. *See id.* at 458.

224. *See Heen, supra* note 155, at 579-90 (collecting cases).

225. *See* H.R. 2491, 104th Cong., 1st Sess. § 13611 (1995). *See* H.R. Rep. No. 280, Vol. II, 104th Cong., 1st Sess. 319 (Oct. 17, 1995) (citing *Schleier* and explaining that the IRS had suspended existing guidance of the tax treatment of damages received for employment discrimination other than age discrimination).

226. *See* H.R. Conf. Rep. No. 350, 104th Cong., 1st Sess. 1452 (Nov. 16, 1995) (explaining that the Senate provision in section 12811 of the Senate bill was the same as section 13611 of the House bill, except that in some cases the exclusion from gross income would apply to punitive damages received in a wrongful death action so long as state law had already provided that only punitive damages may be awarded in a wrongful death action).

227. *See* Omnibus Reconciliation Act of 1995, 104th Cong., 1st Sess. (vetoed on Feb. 29, 1996).

228. *See* H.R. 3448, 104th Cong., 2nd Sess. § 1605 (1996); H.R. Rep. 586, 104th Cong., 2nd Sess. 43 (May 20, 1996) (including in income all punitive damages and damage recoveries for nonphysical injuries).

provision relating to punitive damages.²²⁹ The conference committee adopted the House provision as part of a revenue offset for the Small Business Protection Act,²³⁰ which President Clinton signed into law.²³¹ Thus, seven years after it was first proposed, the amendment became law. The exclusion from gross income under Code section 104(a)(2) now applies to damages “other than punitive damages” received “on account of personal physical injuries or physical sickness.”²³²

Although in this example Congress took action, much time and many legislative resources were expended in the process. Too much reliance on legislative correction in the tax area would waste legislative resources that could be expended in other ways. Furthermore, the adoption of the amendment to section 104(a)(2) depended upon the amendment’s status as a revenue offset for other politically popular tax breaks in a Presidential election year. Congressional action thus depended upon the convergence of a number of factors, including the viability of much larger pieces of legislation to which the amendment was attached.

229. See § 1603 of the Senate Amendment to H.R. 3448, 142 Cong. Rec. S7366, S7385 (daily ed. July 8, 1996) (providing that the exclusion from gross income does not apply to any punitive damages received on account of personal injury whether or not related to a physical injury, except for certain damages awarded in a wrongful death action).

230. See H.R. Conf. Rep. No. 737, 104th Cong., 2nd Sess. 88-89 (Aug. 1, 1996).

231. Small Business Protection Act of 1996, Pub. L. No. 104-188, § 1605, 110 Stat. 1838.

232. As amended, § 104(a) provides in relevant part as follows:

gross income does not include—

(2) the amount of any damages (other than punitive damages) received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal physical injuries or physical sickness

For purposes of paragraph (2), emotional distress shall not be treated as a physical injury or physical sickness. The preceding sentence shall not apply to an amount of damages not in excess of the amount paid for medical care . . . attributable to emotional distress.

26 U.S.C. § 104(a)(2)(1996).

I have argued elsewhere that restricting “personal injuries” to physical injuries would not be the correct fix. See Heen, *supra* note 155, at 606-16. Professor Kahn, in contrast, has argued in favor of limiting the exclusion to physical injuries. See Douglas A. Kahn, *Taxation of Damages after Schleier—Where Are We and Where Do We Go From Here?*, 15 QLR 305, 342 (1995) (concluding that the 1996 statutory amendments “should cure most of the remaining ills in the treatment of damages”); Kahn, *supra* note 208, at 356-58. Although I disagree with Professor Kahn’s view that the policy justification for excluding damages is “weaker when the injury is exclusively nonphysical than when physical injury is involved,” *id.* at 357, I agree that a bright-line standard may be easier to administer than the standards adopted by the Court in *Schleier* and *Burke*.

B. Agency Capture

Professor Schauer has also argued that the plain meaning approach may play an important corrective role in the context of "sometimes-captured" agencies, while acknowledging that its usefulness for that purpose will vary depending upon the context.²³³ Although there may be a need for corrective action if *Chevron* deference is based on an overly optimistic view of the democratic, pluralistic role played by executive agencies, Treasury may be relatively less prone than other administrative agencies to capture by interest groups.²³⁴ As Professor Zelinsky argues, tax administrators are subject to the multiple, sometimes offsetting pressures of a broad range of tax constituencies, giving Treasury and the IRS a greater ability to pursue their regulatory agenda than policymakers dependent for political support on a more narrow or homogeneous range of interest groups.²³⁵ Unlike the environmental context, for example, in which the pro-development and anti-development interests compete against each other for governmental regulatory policy,²³⁶ the tax arena is marked by many competing interests, most with the agenda of lessening their own separate individual or interest group tax burdens. In that arena, the organized interest groups seek tax benefits for themselves, but rarely oppose benefits for each other.²³⁷ Although Treasury is not immune from interest group pressures, it has remained somewhat insulated from the short-term political pressures and constituent needs faced by members of Congress.

If the intuition is correct that the Treasury Department is relatively less subject to capture by regulated interests, and if the plain

233. See *supra* notes 36 & 213.

234. See Daniel Shaviro, *Beyond Public Choice and Public Interest: A Study of the Legislative Process as Illustrated by Tax Legislation in the 1980s*, 139 U. PA. L. REV. 1, 114-115 (1990); see also JOHN F. WITTE, *THE POLITICS AND DEVELOPMENT OF THE FEDERAL INCOME TAX* 382-84 (1985) (suggesting that income tax policymaking be reformed by shifting decisions from the legislative to the executive branch, as was done for tariff changes in the 1930's).

235. See Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions*, 102 YALE L.J. 1165, 1192-94 (1993); see also Ferguson et al., *supra* note 73, at 821-22.

236. See generally, Bradford C. Mank, *Is a Textualist Approach to Statutory Interpretation Pro-Environmentalist?: Why Pragmatic Agency Decisionmaking Is Better than Judicial Literalism*, 53 WASH. & LEE L. REV. 1231, 1233 (1996) (discussing the "frequent conflict in environmental statutes between protecting the public health and limiting the cost of regulation").

237. Shaviro, *supra* note 234, at 55-56 n.254 (noting a "few cases" in which interest groups compete, "as in the longstanding battles between stock and mutual insurance companies or between taxable and tax exempt businesses").

meaning approach provides a check on agency interpretation by captured administrative agencies, then there may be less need for it in the tax context than in some other areas. Greater danger in the tax context may be posed by the possibility that the government would overreach in its efforts to raise revenue than in its capture by particular interest groups.

If government overreaching poses a danger, heightened deference to agency interpretation by the courts may lead to overenforcement of the tax laws rather than to underenforcement. This possibility suggests the need for alternative correctives, such as greater scrutiny of the agency's interpretation by the courts or a less expansive view of delegation to Treasury by Congress. As pointed out by Professor Shaviro in the context of evaluating various possible reforms of the tax legislative process, an executive agency such as Treasury "would not necessarily be good at making political decisions, such as what types of income should be tax-favored."²³⁸ Broader delegation to Treasury "would require a prior political consensus to bar such decisions and restrict the agency's power over implementation."²³⁹ He has concluded that tax reform in 1986 "probably stretched the outer limits of any such consensus."²⁴⁰ As a political matter, therefore, Congress may prefer more narrow specification of the particular contexts in which it delegates legislative-type authority to Treasury.

The above assumptions and intuitions about legislative correction and agency capture need further exploration. My purpose here is merely to raise them as the type of issues that would need investigation before embracing the plain meaning approach as a decision-making procedure in tax cases. At bottom, the resolution of the normative inquiry may depend upon a cost/benefit analysis, taking into account our constitutional values and resource allocation issues as well assessing over a longer period of time the effect of the Court's approach on the development of tax law.

Conclusion

As the above discussion demonstrates, the Supreme Court's evolving approach to statutory interpretation may adversely affect the development of tax law in several ways. Although the Court has been applying the relatively acontextual "plain meaning" analysis in an in-

238. *Id.* at 115.

239. *Id.*

240. *Id.*

creasing number of cases, it does not consistently apply any one approach to statutory interpretation. As suggested by *Burke*, *Schleier*, and *O'Gilvie*, the Court's inconsistent approach to statutory interpretation creates incoherence in the development of tax law.

Even if the Court were to apply the "plain meaning" approach more consistently, problems would remain because of the inherent difficulty of determining textual meanings. Much rides on the Court's initial determination of ambiguity or "plain meaning" because of its deference doctrine, under which the Court defers to reasonable administrative agency interpretation when there are statutory gaps or ambiguities. Inconsistencies in the approach to the ambiguity of statutory language or the applicable deference standard can lead to another form of doctrinal incoherence, in which the Court sometimes interprets a statute based on its "plain meaning" and sometimes defers to administrative interpretation.

Recent Supreme Court tax decisions suggest that there is cause for concern about the effect of the Court's approach to statutory interpretation on the development of tax law. More evidence over a longer period of time would be needed to come to more firm conclusions about such effects. If the early signals represent a pattern that continues, the normative implications must be carefully considered in light of the roles played by the various governmental branches in the development of tax law.

The resolution of the normative inquiry may depend upon a cost/benefit analysis, taking into account constitutional values and the resource allocation issues discussed above. Based upon a preliminary assessment of those issues, including the resource allocation issues raised by reliance on legislative correction and the limited potential for regulatory capture in this context, I conclude that the increased danger of doctrinal incoherence posed by "plain meaning" is not worth the "benefit" of less engagement by the Court (and consequently lessened contentiousness) in tax cases.